

# A Catalyst in the Cotton: The Proper Allocation of the "Goodwill" of Closely Held Businesses and Professional Practices in Dissolution of Marriages

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# A Catalyst in the Cotton: The Proper Allocation of the “Goodwill” of Closely Held Businesses and Professional Practices in Dissolution of Marriages

*[I]nasmuch as you do not object to my taking my hog to Nebraska, therefore I must not object to you taking your slave. Now, I admit this is perfectly logical, if there is no difference between hogs and negroes.<sup>1</sup>*

—Abraham Lincoln, speech on the Kansas-Nebraska Act,  
October 16, 1854

*“Mrs. Truman, Mrs. Truman, I just heard your husband use the word ‘manure.’ Can’t you get him to stop?”*

*“Why, no; it’s taken me 30 years to get him to use that word.”<sup>2</sup>*

—Apocryphal story about President Harry Truman, first attributed to opposition party politics in Wisconsin during the 1948 campaign; many variations of the story abound.

## TABLE OF CONTENTS

I. Introduction .....	1193
II. Background: Goodwill—Origin, Foundation, and Concepts.....	1196
A. Doctrinal Foundations of Property: Patrimonial and Extra-patrimonial Concepts .....	1196
1. The Classification Question: When Is Goodwill “Property?” .....	1196
2. Uncritically Accepted Assumptions .....	1199

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1. Abraham Lincoln, Speech on the Kansas-Nebraska Act (October 16, 1854), available at <http://www.usconstitution.com/AbrahamLincolnonthekansas-NebraskaAct.htm>.

2. Various versions of this tale abound. For the best documented version, although not the exact one given here, see Oral History Interview by James R. Fuchs with Andrew J. Biemiller in Washington, D.C. (July 29, 1977), transcript at 60–61, available at: <http://www.trumanlibrary.org/oralhist/biemiller.htm>. Fuchs had heard several variations of the tale but first learned during this interview that the story arose in a campaign. *Id.* at 61, 62. Biemiller was well positioned to know of these stories; his history, as included in the interview, includes service in the Wisconsin Legislature from 1936–1942 and in the 79th and 81st United States Congresses, as a member from the 5th District of Wisconsin.

3. A Note of Caution . . . . .	1200
B. The Original Goodwill at Common Law . . . . .	1202
1. Initial Definition and Subsequent Development of Goodwill within Law . . . . .	1202
2. Legal Treatment of Goodwill Through the Recent Past . . . . .	1208
C. Broadening of the Goodwill Concept: Multiple Meanings in One Term . . . . .	1210
1. Accounting and Economic Views of Goodwill . . .	1213
2. Importation of "Going Concern" Into "Goodwill" .	1216
D. Goodwill as Currently Employed Within Common Law Divorce Litigation . . . . .	1219
1. The Present "Two Source, Two Effect" Concept . .	1219
2. The Cumulative Impact of Accounting and Economics on Marital Property Concepts . . . . .	1222
E. Clientele in the Civilian Tradition as Seen in Con- temporary French Doctrine . . . . .	1229
1. Scope and Meaning of the Civilian Term "Clientele" . . . . .	1230
2. Effects of Clientele on Marriage Dissolution in Civil Law Jurisdictions . . . . .	1233
III. Analysis: Treatment of Goodwill in Divorce Actions Within Both Traditions . . . . .	1234
A. Clientele and Goodwill: Congruent, Analogues, or Quite Dissimilar? . . . . .	1235
B. Common Law-Based Jurisdictions . . . . .	1235
1. Common Law Without Community Property . . . . .	1235
a. Mississippi, Represented by <i>Singley v. Singley</i> .	1236
b. New York, Represented by <i>Moll v. Moll</i> . . . .	1238
c. New Jersey, Represented by <i>Seiler v. Seiler</i> . .	1240
d. Indiana, Represented by <i>Frazier v. Frazier</i> . . .	1241
2. Common Law With Community Property . . . . .	1242
C. Louisiana: A Mixed Common Law-Civil Law Experience through the <i>Ellington</i> Case . . . . .	1245
1. Issues Presented . . . . .	1245
2. The Holding of <i>Ellington</i> . . . . .	1246
D. The Legislative Response to <i>Ellington</i> . . . . .	1253
1. Tracking the Language of Senate Bill 844 Through the 2003 Regular Session . . . . .	1253
2. What if Louisiana Revised Statutes 9:2801.2 Had Been the Law for the <i>Ellington</i> Trial? . . . . .	1254
3. Has the New Louisiana Revised Statutes 9:2801.2 Resolved the Goodwill Problem in Louisiana? . . . . .	1255

IV. Conclusion and Recommendations ..... 1255

    A. The Superior Civilian Rationale Underlying  
       “Clientele” ..... 1255

        1. The “Source-Effect” Concept Should be  
           Abandoned. .... 1256

        2. The Goodwill Concept, as Applied in Law,  
           Should not be Merged with Either “Going  
           Concern” or “Non-competition” Agreements. ... 1257

    B. Louisiana Revised Statutes 9:2801.2 Should Be  
       Amended to Delete or Qualify the Word “Solely”. ... 1257

    C. A Few Final Reflections ..... 1260

Appendix A

    The Louisiana Second Circuit Court of Appeal's Recitation of the  
    *Ellington* Trial Court's Valuation Methodology and Findings for  
    the Noble Ellington Cotton Company, Inc. .... 1262

Appendix B

    The Court of Appeals of Iowa's Affirmation of the Iowa District  
    Court for Polk County's Findings and Holding in *In re the*  
    *Marriage of Ceilley*. .... 1263

I. INTRODUCTION

Noble Ellington, Jr. and Peggy McDowell married in 1964. They jointly owned and operated a cotton brokerage firm, the Noble Ellington Cotton Company, Incorporated (NECC), for more than thirty years before finally divorcing in 1998.<sup>3</sup> The most hotly contested issue in their property settlement was the proper allocation and value of the family cotton business. The *Ellington* case turned upon the treatment and value of the goodwill of their brokerage firm, arguably a key element in determining the company's value.<sup>4</sup> The positions of the parties were not directly opposed at trial nor on

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3. *Ellington v. Ellington*, 36,943 (La. App. 2d Cir. 2003), 842 So.2d 1160, 1163.

4. The reported case shows that the term “goodwill” was never defined by either expert witnesses, by the trial court, nor by the appeal court. The term was discussed by the experts, who disputed both its presence and its value. The Second Circuit, “[h]aving reviewed extensively the jurisprudence regarding goodwill and the propriety of its inclusion in the value of a community corporation such as NECC,” affirmed the trial court's holding, noting that “valuation of the Ellingtons’ business should include consideration of an intangible value predominantly attributable to NECC’s customer base.” *Id.* at 1170.

appeal. Mr. Ellington argued, in essence, that the family business had no value apart from him.<sup>5</sup> Mrs. Ellington, to a somewhat less theoretical approach, argued instead that the court must rely entirely upon one side's experts or the other's, and thus could not mix portions of each expert's views to craft a partition of their community property.<sup>6</sup> Ultimately, the trial court allocated NECC to Mr. Ellington and compensated Mrs. Ellington for half of its value, for a sum of \$146,500.<sup>7</sup> The court derived that value from a combination of each expert's conclusions.<sup>8</sup>

The trial court's written reasons for judgment concluded that the family cotton business "can and does have an intangible asset value and whether that intangible value is termed goodwill, customer base or something else is not important. What is important, and also much more difficult, is using intangible value in determining the total value of the business."<sup>9</sup> Both parties appealed but the Louisiana Second Circuit Court of Appeal upheld the decision, stating that the trial court did not abuse its discretion in crafting a hybrid value from parts of each expert's calculations.<sup>10</sup>

Actually, whether the "intangible value" that the trial court weighed is termed "goodwill," "customer base," or "something else," is *supremely* important. This comment's principal thesis is that personal goodwill cannot be correctly classified as a marital asset in either a common or a civilian law jurisdiction.<sup>11</sup> By contrast, the goodwill attributable to a distinct business or professional entity is properly subject to a regime of community property in both jurisdictions.

The following two major tenets support the thesis that personal goodwill cannot legitimately fall into community property: 1) The common law's concept of goodwill, as applied in divorce matters, is

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5. *Id.* at 1166, 1168.

6. *Id.* at 1166.

7. *Id.* at 1164-65.

8. *Id.*

9. *Id.* at 1170.

10. *Id.* at 1164-65, 1171, 1175.

11. Note that the "gay marriage" debate arising from *Goodridge v. Department of Public Health*, 798 N.E.2d 941 (Mass. 2003), does not affect this comment. The sex of the other spouse will not affect goodwill, nor will the number of spouses because under this proposal no one can hold a property interest in the personality of another as valued in goodwill. Similarly, if the "effort, skill, and industry" of a spouse is distinguishable from the things produced by that "effort, skill, and industry," then the number or sex of the spouse(s) will not change the disposition of goodwill. Note that the Louisiana Civil Code defines community property, in pertinent part, as "property acquired . . . through the effort, skill, or industry of either spouse." La. Civ. Code art. 2338. Article 2338 does *not* place that "effort, skill, or industry" itself into the community.

both too broad and too narrow. This conceptualization mixes “personal” with “commercial” and “professional” (which is too broad). It also encompasses only a portion of “commercial” goodwill’s true scope (which is too narrow), since it lacks the civil law concept of “introduction.” 2) That component of both professional and commercial goodwill arising from one’s personality is exclusive to its possessor. It is thus separate property that should not devolve into the community.

Within Louisiana, Louisiana Revised Statutes 9:2801.2 attempted to exclude personal goodwill from community property when such goodwill results “solely from the identity, reputation or qualifications of the owner or from his relationship with clients or customers of the business.”<sup>12</sup> Yet, one must assess the 2003 version of Louisiana Revised Statutes 9:2801.2 as “unsuccessful” because the word “solely” negates the new law whenever any portion of the goodwill, however slight, results from any person other than the owner. Accordingly, “solely” should be deleted or amended with a qualifier.

The *Ellington* case raises a multitude of perplexing theoretical questions, the answers to which carry serious practical implications. For example, just what is this “goodwill” so strongly contested in *Ellington*? Is the “goodwill” of a professional practice, such as law or medicine, different in any legally meaningful way from the goodwill of an ordinary business? Is either type of goodwill even a thing, such that it can be “property,” at all? If so, is this intangible property divisible? If it can be divided, should it be divided? (A civilian would pose the question as, “Is it susceptible of partition?”) If personal goodwill can and should be divided between the spouses, on what basis is it best apportioned? If it cannot be divided, should the other spouse be compensated in some manner for goodwill of the family business? For any of the personal goodwill of the other spouse? These difficult issues surrounding the unique nature and proper allocation of goodwill serve as the focus of this comment.

The Background section begins by considering the theoretical foundation of goodwill within the framework of property law (Part II.A.). A review of some threshold classification issues often uncritically accepted follows, ending with a note of caution about the

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12. Louisiana Revised Statutes 9:2801.2 took effect on August 15, 2003. Senate Bill 844 of the 2003 Regular Session became Act 837 when signed into law by Governor Foster on July 1, 2003. See 2003 La. Acts No. 837, at Appendix 7. However, as a result of an earlier draft of this comment, Revised Statutes 9:2801.2 was amended as suggested here in 2004. The current law took effect on August 15, 2004. See 2004 La. Acts No. 177, at Appendix 11. The full story of how “solely” changed from “primarily” into the extensive revision finally passed must wait for another day. Suffice it to say that “primarily” was as unfair in one direction as “solely” was in the other.

limited ability of the law to resolve value judgments. The next section, Part II.B., traces the evolution of the concept of goodwill from its birth in commercial contracts at common law. The shifting content of goodwill in common law jurisdictions as the term expanded in scope over the last few decades is the subject of Part II.C. Part II.D. then turns to the latest iteration of goodwill and explores its use in modern common law divorces. An examination of the civil law concept of "clientele" forms Part II.E., the last Background section.

The Analysis section begins by contrasting and comparing the civilian doctrine of clientele with goodwill in Part III.A. Treatment of the goodwill of closely held family businesses and professional practices is then examined in three types of jurisdictions: (1) Common law states without community property (Part III.B.1.); (2) Common law states with community property (Part III.B.2.); and (3) Louisiana, a "mixed jurisdiction" whose law is largely derived from—and still heavily influenced by—the civil law tradition (Part III.C.). This section devotes particular emphasis on one Louisiana case, the property settlement in *Ellington*. A discussion of Louisiana's legislative response to *Ellington* completes the Analysis Section in Part III.D.

The Conclusion section, Part IV, contains both general recommendations for matters of concept and doctrine (Part IV.A.) as well as recommendations for addressing specific Louisiana issues raised by *Ellington* and reflected in the newly enacted Louisiana Revised Statutes 9:2801.2 (Part IV.B.). "A Few Final Reflections" completes the comment as Part IV.C.

## II. BACKGROUND—GOODWILL: ORIGIN, FOUNDATION, AND CONCEPTS

### *A. Doctrinal Foundations of Property: Patrimonial and Extra-patrimonial Concepts*

#### *1. The Classification Question: When Is Goodwill "Property?"*

Before the *Ellington* case and the issues it highlights can be profitably explored, the scope of the problem being investigated must be both explicitly delineated as well as placed in its proper context. Since personal goodwill can exist in both a closely held family business and in a professional practice, the allocation and division of personal goodwill must be evaluated regardless of where it may be found.

The classic civilian approach to analyzing the role, mission, and nature of a concept begins with assigning it to a specific location in a taxonomy, within a codified system of law.<sup>13</sup> There is no point in pondering how to value a thing until it can be established that the thing under scrutiny is "property." Once it is recognized to be property, there is no point in attempting to divide it unless the judge can be confident that it is community property. If it is separate property, then only one spouse can own it, regardless of its susceptibility to division. Thus, the only circumstance in which there is work to be done by a fact finder is when a thing is both property and subject to a claim by both spouses. Attempting to divide a thing before confirming that it is, in fact, both property and divisible is the difference between "doing a thing right" and "doing the right thing."<sup>14</sup>

Distinguished Louisiana commentators have previously discussed the "property or not property" aspect of the goodwill problem. Professors Spaht and Hargrave, in the *Louisiana Civil Law Treatise*, observed that "[s]ome things are so intimately a part of one's body or one's personality" that they cannot be "shar[ed]" with another person.<sup>15</sup> This property-patrimonial-extra-patrimonial distinction is most difficult to apply to someone's personal qualities in divorce litigation. They note that the "inquiry . . . goes beyond a definitional approach" and thus "considers a broad range of . . . history and policy concerns," with professional goodwill among the most current controversies.<sup>16</sup>

"Patrimonial" is an alien term, but not an unknown concept, to the common law. It is half of a pair. Its (fraternal) twin is "extra-patrimonial." The "patrimony" of a person is the sum total of

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13. See John H. Tucker, Jr., *Foreword* to Louisiana Civil Code (West 2004): What is meant by the term 'code' as we use it here [referring to Louisiana's Civil Code] is to designate an analytical and logical statement of general principles of the law to be applied by deduction to specific cases and extended by analogy to cases where the aphorism "*au-delà du code mais par le code civil*" ("beyond the civil code but through the civil code") can be applied.

14. "Peter F. Drucker once differentiated between doing things right and doing the right thing:"

Doing things right has to do with efficiency, hence knowledge. Doing the right thing has to do with effectiveness, hence wisdom. Much of the knowledge I see being transmitted and shared is about efficiency, not effectiveness. *The righter we do the wrong thing, the wronger we become.*

Russell Ackoff, *Commentary*, 1 Reflections: The SoL Journal 56 (1999) (emphasis added).

15. Katherine Shaw Spaht & W. Lee Hargrave, *Matrimonial Regimes* § 2.1, in 16 Louisiana Civil Law Treatise (1997).

16. *Id.*



everything that person owns (or owes) with any economic value.<sup>17</sup> If it can be bought, sold, or repaid, it is patrimony. However, some things are enforceable as rights and duties, yet either cannot be reduced to an economic value or their use for economic purposes is illegal or otherwise contrary to public policy. These impossible or forbidden rights and duties are "extra-patrimonial."<sup>18</sup> For example, one has a right to marry. Once married, rights and duties accrue. However, being married is an extra-patrimonial thing. No one can "sell" a marriage.<sup>19</sup> While some pose the question as "whether an asset is 'property' or whether it is 'patrimonial,'" the better distinction is not between "property" and "patrimony" but rather between "property" and "non-property."<sup>20</sup>

Spaht and Hargrave further develop the very important distinction between property and non-property by noting that "one's ability to work and enjoy the fruits of his labor" is a valuable property right nonetheless protected from, for example, "seizure by creditors," yet that same ability to work "would not be part of the community,"

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17. Gérard Cornu, *Droit Civil: Introduction, Les Personnes & Les Biens*, nos. 55-56, 30 (4th ed. 1990) (translated by J.R. Trahan, 1997).

18. "Certain rights have no pecuniary value." Alex Weill & Francois Terré, *Droit Civil: Introduction Général*, nos. 241, 255 (4th ed. 1979) (translated by J.R. Trahan, 1997).

19. *Id.* "Different from patrimonial rights, extra-patrimonial rights are nontransferable, intransmissible, unseizable, and imprescriptible." *Id.* The right to marry is extra-patrimonial. Spaht and Hargrave also cite French commentators wrestling with the disposal of personal rights, saying: "Aubry and Rau suggest that, except for rare cases, the distinction between patrimonial and extra-patrimonial rights is in reality a distinction between rights which their subject may dispose of and those which he may not. The extra-patrimonial interests can not be expressed in currency because there is no market offering a current price for them." Spaht & Hargrave, *supra* note 15, § 2.4. Examples given by Aubry and Rau of extra-patrimonial rights include the rights resulting from marriage; rights derived from paternity and status as head of family; the right of one to his own body and name; and the intellectual right of an author to a work of art. *Id.* (citing Aubry & Rau, II *Droit Civil Français* § 162, (P. Esmein 7th ed. 1961), in 2 *Civil Law Translations* (La. State L. Inst. 1966)).

20. Spaht and Hargrave note that "[t]he Continental concept of patrimony and its distinction between patrimonial and extra-patrimonial rights has been called 'a distinction that has given rise to doctrinal controversies and has proved to be analytically deficient.'" Spaht & Hargrave, *supra* note 15, § 2.4 (citing A.N. Yiannopoulos, *Property* § 127, in 2 *Louisiana Civil Law Treatise* (2d ed. 1980)). Be that as it may, since this comment only examines the personal goodwill associated with closely held businesses and professional practices in divorces, the distinction's deficiencies in some other contexts are not a limiting factor here. Moreover, Weill and Terré concede that the distinction is not "absolute" and "sometimes lacks precision," although they maintain that "the distinction corresponds to reality: certain rights have a pecuniary value while others have a moral value." Weill & Terré, *supra* note 18, no. 241. Perhaps a better phrase would be "have *only* a moral value?"

especially not for “wages earned after the termination [of the community]” because such wages are separate property.<sup>21</sup> Perhaps these difficulties in assessing what is property at all, much less what property is then subject to claims by more than one person, explain why these issues are so often assumed away.

## 2. *Uncritically Accepted Assumptions*

Unfortunately, much (if not most) of the commentary on marital and community property does not squarely address whether personal goodwill is divisible or not during divorces. Instead, the commentators tend to focus on problems that should come a step or two later in the analysis sequence.<sup>22</sup> For example, arguments over which accounting method is best suited for weighing the proper division of a professional practice (usually in law or medicine) simply presume (a) that there is such a “thing” within the community and (b) that this thing is subject to division.<sup>23</sup> No point is served by interminable accounting debates over the best means to divide an indivisible thing, especially a thing that is not legitimately subject to the jurisdiction of a court. Regrettably, many cases, as well as many of the law reviews and explanatory articles for attorneys, begin with the uncritically accepted assumption that personal goodwill is subject to partition in a divorce. The bar journals are especially prone to address the finer points of valuation methods without pausing to

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21. Spaht & Hargrave, *supra* note 15, § 2.4.

22. Allen M. Parkman, *A Systematic Approach to Valuing the Goodwill of Professional Practices*, in Ronald L. Brown, *Valuing Professional Practices and Licenses* 6-1, 6-1 (3d ed. 1998), available at <http://www.unm.edu/~parkman/Goodwill.PDF>.

23. See, e.g., Bryan Mauldin, *Identifying, Valuing, and Dividing Professional Goodwill as Community Property at Dissolution of the Marital Community*, 56 Tul. L. Rev. 313 (1981) (failing to appreciate the indispensable step of determining whether the property is divisible in the analysis of goodwill). Another recent comment forthrightly disparages any attempt to consider property rights, opining that “engaging in an essentialist inquiry into the nature of property simply masks the inherent normative choices.” Carolyn J. Frantz & Hanoach Dagan, *Properties of Marriage*, 104 Colum. L. Rev. 75, 109 (2004). *Au contraire*, Mesdames; mes aimés. The only things “masked” here are the common law’s lack of (1) rigor and (2) a taxonomy.

consider if the enterprise itself is legitimate.<sup>24</sup> Both trial and appellate courts have also displayed this tendency.<sup>25</sup>

Valuation of an intangible (an "incorporeal" to a civilian) such as goodwill in any business is problematic even under the "ideal" condition of an arm's length sale to a third person. Valuing the typical closely held family business is even more difficult. Valuing a professional practice or a family business in a divorce is most difficult of all, since there is no willing buyer and seller and no disinterested outside party making the purchase.<sup>26</sup>

### 3. A Note of Caution

One caveat to keep in mind throughout this comment: many of the problems discovered in this research effort are not truly "legal" problems. A question posed as "Does the goodwill arising from someone's professional practice fall into the community?" probably does appear to be only a legal question. However, asking the identical question with other words yields a far different result. If the identical issue is instead presented as "Can someone's personal qualities be owned by another person?," does it still seem to be only a legal question?

At the end of the day, the controversy over personal, commercial, and professional goodwill is not one which can be resolved by

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24. See, e.g., Michael W. Kalcheim, *Expert Testimony and Valuing Goodwill at Divorce*, 88 Ill. B.J. 652 (2000); Robert W. Levis, *Valuation of Businesses in Colorado Divorces*, Colo. Law., June 2003, at 73; Allen M. Parkman, *Human Capital as Property in Divorce Settlements*, 40 Ark. L. Rev. 439 (1987). See also Allen M. Parkman, *Human Capital as Property in Celebrity Divorces*, 29 Fam. L.Q. 141 (1995); Allen M. Parkman, *A Systematic Approach to Property in Divorces*, 12 Fam. Advocate 34 (1989) [hereinafter Parkman, *A Systematic Approach*]; Allen M. Parkman, *The Treatment of Professional Goodwill in Divorce Proceedings*, 18 Fam. L.Q. 213 (1984). An expert in *Ellington* believed a step had been skipped: "According to Mr. Clark, the company's [NECC] goodwill is personal and therefore should not be considered." *Ellington v. Ellington*, 36,943 (La. App. 2d Cir. 2003), 842 So. 2d 1160, 1164 n.5.

25. On appeal the *Ellington* panel considered the challenge to partitioning personal goodwill but followed an earlier business goodwill case, *Godwin v. Godwin*. *Ellington*, 842 So. 2d at 1170 (citing *Godwin v. Godwin*, 533 So. 2d 1009 (La. App. 1st Cir. 1988)). The Louisiana Fifth Circuit Court of Appeal recently reached the same conclusion as the Second Circuit in *Schrio v. Schrio*, 02-542 (La. App. 5th Cir. 2003), 839 So. 2d 304 (La. App. 5th Cir.). *Godwin* and *Schrio* both hold that personal goodwill is a divisible marital asset—a thing which falls into the community—when it is attached to a commercial corporation, but not when it is attached to a doctor's or lawyer's professional practice corporation.

26. For example, one expert in *Ellington* testified that "in a divorce situation when you're settling property its [sic] very rare to have a willing seller . . ." and "this is for property settlement purposes, you don't have to have a willing buyer or a willing seller." *Ellington*, 842 So. 2d at 1167-68.

lawyers, judges, and scholars alone. It is a values conflict, not a legal question. Both case law and commentary are so widely split that reliance upon finding "the answer" in any court room is misplaced. No judge has an envelope on the bench containing "Colonel Mustard in the Billiard Room with the Candlestick."<sup>27</sup>

Legal training can be of tremendous help in highlighting various facets of an issue and exploring the consequences of different outcomes. However, legal scholarship can only point the way to a solution. Choosing the "correct" solution is another matter entirely. Ultimately, in democratic societies, only the court of public opinion—expressed at the ballot box—can truly settle values questions. The Louisiana Supreme Court was keenly aware of this "values-law" distinction when it observed:

[A court errs] in allowing its own policy determination to override the policy determination made by the legislature. It is not the prerogative of the judiciary to disregard public policy decisions underlying legislation or to reweigh balances of interests and policy considerations already struck by the legislature. It is not our role to consider the wisdom of the legislature in adopting the statute. It is our province to determine only the applicability, legality, and constitutionality of the statute.<sup>28</sup>

Put another way, do values drive law, or does law drive values?<sup>29</sup> Did hearts and minds change in America as a result of something like the landmark Civil Rights Act of 1964? Or, did the law change because American hearts and minds had changed? Perhaps the "thesis behind the thesis" of this comment is the bedrock belief that

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27. Of course the reference is from the popular American board game "Clue."

28. *Soloco v. Dupree*, 1997-1256 (La. 1998), 707 So. 2d 12, 16. The United States Supreme Court said essentially the same thing in *Chevron U.S.A., Inc. v. Natural Resources Defense Council*, 467 U.S. 837, 866, 104 S. Ct. 2778, 2793 (1984) (quoting *TVA v. Hill*, 437 U.S. 153, 195, 98 S. Ct. 2279, 2302 (1978)):

When a challenge to an agency construction of a statutory provision, fairly conceptualized, really centers on the wisdom of the agency's policy, rather than whether it is a reasonable choice within a gap left open by Congress, the challenge must fail. In such a case, federal judges—who have no constituency—have a duty to respect legitimate policy choices made by those who do. The responsibilities for assessing the wisdom of such policy choices and resolving the struggle between competing views of the public interest are not judicial ones: "Our Constitution vests such responsibilities in the political branches."

29. For an expanded discussion of the interrelationship between law, culture, and values, see Katherine Spaht, *The Last One Hundred Years: The Incredible Retreat of Law from the Regulation of Marriage*, 63 La. L. Rev. 243, 245-47.

law is meant to serve and protect values, not that societies have values in order to serve law.

### *B. The Original Goodwill at Common Law*

#### *1. Initial Definition and Subsequent Development of Goodwill Within Law*

The initial case establishing goodwill as an asset of a business doubles as another good example of the interrelationship between values and law. At common law, the legal definition of the term "goodwill" first appeared in *Cruttwell v. Lye*, an English case from 1810, as "[t]he goodwill, which has been the subject of sale, is nothing more than the probability that the old customers will resort to the old place."<sup>30</sup> Lye's freight business had gone bankrupt. Cruttwell bought "Lot 1 as the carrying business of George and Edward Lye; together with the goodwill of the extensive premises in Broad Street, Bath."<sup>31</sup> Later, after new financing, Lye again offered wagon deliveries "at the usual hours" although not by exactly the same route as before. Lye and his son also solicited their former customers. Cruttwell then moved for an injunction restraining the bankrupt Lye and his son from carrying on his trade.<sup>32</sup>

This contract dispute turned on two questions: (a) exactly what had Cruttwell bought? and (b) did that sale impinge upon Lye's personal rights? Lord Eldon, presiding in this equity matter as Lord Chancellor, settled the first question when he observed that Lye had set up his revived freight wagon business as like, but not the same as, the trade sold.<sup>33</sup> As to the second question, Lye's counsel argued that his personal rights could not be "deprived by the assignees, or any other person" so Lye's right to resume his business was not "forfeited by the bankruptcy . . . [and] . . . could not be disposed of."<sup>34</sup>

This old English case is an eerie foreshadowing of the "personal qualities" or "community property" tension found at the heart of good will disputes in modern divorce cases (which will be fully developed and demonstrated in Part II.D.). Lord Eldon, in 1810, saw the gravity of the values conflict these issues presented in this apparently simple

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30. 34 Eng. Rep. 129, 134 (Chan. 1810).

31. *Id.* at 130. Note most carefully that the Bankruptcy Court sold Cruttwell two different things; "the business" itself and the "goodwill of the extensive premises in Broad Street, Bath." Note also that the goodwill sold was "of the extensive premises" at a specific location. It was not attached to nor formed by any personal quality, neither of Lye nor of his son. *Id.*

32. *Id.*

33. *Id.* (emphasis original).

34. *Id.*

case and enunciated them quite clearly in his opening paragraph. He observed:

[o]n the one hand, if this court does not interpose, the Plaintiff cannot possibly have what he really intended to purchase: on the other hand, if the Defendant has a right to carry on this trade, I should by interfering destroy that right to an extent, which I could never remedy.<sup>35</sup>

In the absence of either fraud or a non-compete agreement, Lord Eldon could find no rationale to grant the injunction. "Fraud," he wrote, "would [lead to a very different result]; but if [fraud] . . . is prevented [only by] . . . means . . . which belong to . . . the fair course of a [lawful] trade, . . . I should, by interposing, carry the effect of injunction to a much greater length than any decision has authorised, or imagination ever suggested."<sup>36</sup>

English case law that is almost 200 years old requires a bit of careful parsing, but a fair contemporary reading of the 1810 conclusion, based upon the whole reported case, might be,

If Lye had pretended to be Cruttwell, then that fraud could justify an injunction. However, Lye has a right to conduct a lawful business. Interfering in Lye's personal freedom, where there is no non-compete agreement, would stretch an injunction far beyond its rightful limits. As between personal freedom and the benefits of a contract, on these facts, freedom must prevail.<sup>37</sup>

Meanwhile, in the United States, Justice Joseph Story wrote an oft-cited, more elaborate definition of goodwill than that found in *Cruttwell*. Section 99 of his 1841 treatise on partnership, which has been cited in innumerable cases as an all-encompassing definition of goodwill, is actually not Justice Story's final word on the subject. The part of section 99 that is invariably cited as his view of goodwill is:

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35. *Id.* at 134.

36. *Id.* at 131–32. Lord Eldon noted that the parties had no "covenant" not to "engage in such trade." *Id.* at 132. Fraud was twice rejected. *Id.* at 133–34. A law professor once observed "there are no solutions . . . only issues that are fought out again and again." William F. Harvey, Speech to the Staff of the Legal Services Corporation in Washington, D.C. (March 4, 1982), *quoted in* Alan Houseman & John Dooley, Legal Services History 4–17 n.61 (1984). The modern reach of business goodwill into community property settlements confirms Professor Harvey's "endless struggle" sentiment.

37. Of course, anyone having read the complete *Cruttwell* case is welcome to construct an alternate modern text as though Lord Eldon were rendering his opinion today.

an advantage or benefit which is acquired by an establishment, beyond the mere value of the capital, stock, funds or property employed therein, in consequence of the general public patronage and encouragement which it receives from constant or habitual customers, on account of its local position, or common celebrity, or reputation for skill or affluence, or punctuality, or from other accidental circumstances or necessities, or even from ancient partialities or prejudices.<sup>38</sup>

However, Justice Story was writing of *partnerships*, not about other business combinations, much less about any family law matter. After a review of several types of partnerships, he made a further observation that cannot be regarded as anything less than devastating to those who wish to ascribe *business* goodwill to *personality*: "It seems that good will can constitute a part of the partnership effects or interests only in cases of mere commercial business or trades, and not in cases of professional business, which is almost necessarily connected with personal skill and confidence in the particular partner."<sup>39</sup>

Moreover, the court in *Douthart v. Logan*, after quoting Justice Story's treatise then immediately cited a second mid-nineteenth century treatise,<sup>40</sup> which raises an equally insurmountable obstacle to the "business good will attaches to personality" position. The court was impressed by Parson's

distinction . . . taken between "the good will of a partnership in trade and that of a professional partnership. [Professionals] may become partners; but the good will attached to [them] must be considered more as a personal [thing] than as a local thing. It is not a probability that the old customers will go to the old place, but to the same persons, wherever they may be."<sup>41</sup>

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38. Joseph Story, *Commentaries on the Law of Partnership as a Branch of Commercial and Maritime Jurisprudence: with Occasional Illustrations from the Civil and Foreign Law* (1841).

39. *Douthart v. Logan*, 86 Ill. App. 294, 310 (Ill. 1st Cir. 1899), *aff'd.*, 60 N.E. 507 (Ill. 1901) (quoting Joseph Story, *Commentaries* (7th ed. 1881)).

40. "In *Parsons on Part.*, the author says, in speaking of good will and the difficulty of giving a definition thereof, that . . . the definition of good will . . . from Lord Eldon, 'is an exact statement of the legal meaning of good will.'" *Id.* Curiously, two different Parsons wrote partnership treatises in the late nineteenth century. Theophilus Parsons wrote *A Treatise on the Law of Partnership*, while James Parsons wrote *An Exposition of the Principles of Partnership*. The *Douthart* court cited Theophilus, not James, Parsons because James Parsons did not quote *Cruttwell*.

41. Theophilus Parsons, *A Treatise on the Law of Partnership* 239 (Joseph Henry Beale, Jr. ed., 4th ed. 1893).

Moreover, Theophilus Parsons explicitly considered, but rejected, the “objection” that good-will “be altogether dependent upon place, and [thus] wholly independent of persons,” preferring instead the “kind and friendly feeling of others,” which he felt Lord Eldon’s classic *Cruttwell* definition had captured as “the true technical and legal meaning of the word [good-will].”<sup>42</sup> Parsons explained in the footnote citing *Cruttwell* that good-will was legally recognized as a locality only and not any personality because it left the seller of the business “at liberty to set up the same trade in any other situation.”<sup>43</sup>

The next milestone in the development of goodwill at common law occurred in England in *Smith v. Everett*.<sup>44</sup> Smith was one of two partners in a bank. When Smith died, Everett, the surviving partner, put the bank up for sale. The buyers discovered under the English banking laws then in effect that they could not issue bank notes unless Everett remained with the new firm. He agreed to stay on for one year, serving as an active manager during the first six months. Smith’s widow, unsatisfied with Everett’s accounting of the bank’s books, sued him. She also asked for an increased share of the sales price, believing at least some of the bank’s value was goodwill.<sup>45</sup> If so, some part of the goodwill should fall into her late husband’s estate as a partner in the bank. Everett countered by saying that the goodwill had no value whatever since, by itself, it would not have included the building, any stock in the bank, any right to issue bank notes, or any restriction of his right to remain in the banking business in the same building.<sup>46</sup>

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42. *Id.*

43. *Id.* at 239 n.8.

44. 27 Beav. 446 (1859). *Smith* is one of the cases “from the year 1785 as are still of practical utility.” 72 Rev. Rep. 484 (1911) (reprinting *Smith*). At least one goodwill rule of *Cruttwell*—that any non-compete agreement must be express—was intact and still functioning in England in 1911, a full century later. *See id.*

45. 27 Beav. at 448.

46. *Id.* at 450.



The Master of the Rolls<sup>47</sup> hearing the case, Sir John Romilly,<sup>48</sup> reached one key conclusion in the first substantive paragraph of the opinion, “entertain[ing] no doubt” that a proportionate “share of the goodwill (where it is of any value at all) . . . [is a] part of the estate of the deceased partner . . . .”<sup>49</sup> Here, that would be half, from the universal “Black Letter Law” that partners share equally, without regard to such factors as which one does more of the work or recruits more customers, and so on.<sup>50</sup>

However, in the very next sentence, Sir John continued to say that any goodwill interest “must be limited by the rights of the surviving partner, and the consequences which . . . follow from the death of one of the partners.”<sup>51</sup> One such right, according to Sir John, is “no one would have had any right to prevent [the surviving partner] from carrying on the very same business on the very same

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47. The “Master of the Rolls” is the chief of the Civil Division of the Court of Appeal. See Kevin’s English Law Glossary, *Master of the Rolls*, at [http://www.kevinboone.com/lawglos\\_Master\\_of\\_the\\_Rolls.html](http://www.kevinboone.com/lawglos_Master_of_the_Rolls.html). The position fills the third seat of the Supreme Court of Judicature in England. The other two members are the Lord Chancellor (the president of the Chancery Division) and the Lord Chief Justice (president of the Kings Bench Division). See The 1911 Edition Encyclopedia, *Master of the Rolls*, at [http://13.1911encyclopedia.org/M/MA/MASTER\\_OF\\_THE\\_ROLLS.htm](http://13.1911encyclopedia.org/M/MA/MASTER_OF_THE_ROLLS.htm). The incumbent Master of the Rolls in June, 2003 was Lord Phillips. He described a few of his duties in a keynote speech given at two Law Society Litigation Conferences:

It is now nearly three years since I took up my duties as Master of the Rolls. When I did so I was not quite sure what the Rolls were of which I was Master. I had, as have many people, a vague idea that they were included on the roll of solicitors. That is not the case. The office of Master of the Rolls originates in the 13th century long before solicitors existed. He was assistant to the Chancellor, who was then the King’s Chaplain and secretary. The Master of the Rolls was also a cleric. His task was to look after the King’s official correspondence which was recorded on parchment rolls and as a legacy of that task I still chair the committee which advises the Lord Chancellor on Public Records. I have nonetheless many duties in relation to your profession and I see my role as essentially avuncular.

Lord Phillips, Master of the Rolls, Keynote Speech at the Law Society Litigation Conferences (June 5, 2003 & June 19, 2003), available at <http://www.lcd.gov.uk/judicial/speeches/lp190603.htm>.

48. Historical point of curiosity: Sir John Romilly’s father, Sir Samuel, represented the unsuccessful Crutwell thirty-nine years earlier in the original “goodwill” case. See The 1911 Edition Encyclopedia LovetoKnow, *John Romilly, 1st Baron Romilly*, at [http://29.1911encyclopedia.org/R/RO/ROMILLY\\_JOHN\\_ROMILLY\\_1ST\\_BARON.htm](http://29.1911encyclopedia.org/R/RO/ROMILLY_JOHN_ROMILLY_1ST_BARON.htm).

49. *Smith*, 27 Beav. at 452.

50. For example, the Uniform Partnership Act of 1914 reads, “subject to any agreement between them . . . each partner shall . . . share equally in the profits . . . after all liabilities.” Uniform Partnership Act of 1914 § 18.

51. *Smith*, 27 Beav. at 452.

premises as before," even if he somehow lacked the right to continue business under the same name.<sup>52</sup>

This follows one rule of *Cruttwell*: only an express covenant not to compete can restrict the right to remain in (or reenter) a line of trade. However, the other rule of *Cruttwell*, that goodwill is only the chance of future business from old customers, is also repeated in *Smith*. Sir John wrote that, since Everett could carry on with the name "Old Sarum Bank," the value of the goodwill, "under the name . . . 'New Sarum Bank,' with the chance of retaining the customers of the former Bank, was exceedingly small, not to say infinitesimal."<sup>53</sup>

While Sir John was quite confident of the controlling law in the *Smith* case, he was greatly troubled by the scant evidence presented. The legal principle that goodwill had a marketable value and could thus be sold was not disputed. His problem in the case was his inability to determine, from the facts before him, if any portion of Smith's goodwill had been included in the original sale price of £10,000 for the entire bank. After a subsequent special inquiry, he held that the sale price had not included anything for goodwill, and so Sir John awarded the widow £2,000 for Smith's half of the goodwill. Her other claims, primarily the alleged mismanagement by Everett, were all denied.<sup>54</sup>

Looking back at this 1859 case through modern eyes, and from the vantage point of goodwill in divorces, several aspects of Sir John Romilly's holdings impinge upon the modern attempt to import goodwill into family law. First, observe that Smith's personal qualities played no role whatsoever in the case. Whatever goodwill existed in the bank's assets only attached to the bank and not to either partner. Smith's widow was entitled to Smith's share simply because he had been a partner. Second, no personal quality of hers factored into the goodwill, either. She now owned half the bank, so she owned half of the bank's assets, which included half the goodwill. Neither Everett nor Smith's widow inquired into any personal relationship in this matter. The presence or absence of her support of Smith during their marriage was irrelevant. Third, the goodwill was not valued by how much it was worth to the surviving partner. It was worth what a buyer would pay for the bank. Thus, goodwill operated solely through commercial transactions, was not bound up in any personal qualities, and was valued only by what a buyer would pay for it.

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52. *Id.*

53. *Id.*

54. *Id.* at 456.

## 2. *Legal Treatment of Goodwill Through the Recent Past*

Some measure of the stability and power of common law precedent may be gauged by the fact that, 151 years after *Cruttwell v. Lye*, and within the mixed common law-civil law jurisdiction of Louisiana, the Fourth Circuit Court of Appeal nevertheless held "[the] rule is that, in the absence of an expressed stipulation to the contrary in the contract, the sale of a business with the goodwill thereof does not prevent the vendor from engaging in a similar business in the same vicinity or elsewhere."<sup>55</sup>

Moreover, the Ohio Supreme Court, seventy-one years after *Cruttwell* and twenty-two years after *Smith*, upheld an express non-compete clause in a contract of sale for a business and its attached goodwill.<sup>56</sup> This 1881 case, *Morgan v. Perhamus*, makes two more noteworthy points. First, *Morgan* found Sir John's reasoning in *Smith v. Everett* to be persuasive authority for the proposition that "the good-will of a trade or business, *when connected to it*, is property."<sup>57</sup> Goodwill, as originally understood, had no independent existence apart from a business and was therefore never a "personal" thing. Second, *Morgan* contained a citation from yet another mid-nineteenth century common law treatise (this one from England) that displayed the consistent point of view at common law, explaining the term "goodwill" as "generally used to denote the benefit arising from connection and reputation, and its value is what can be got for *the chance of being able to keep that connection* and improve it. . . . [The goodwill of] an established business . . . has . . . marketable value, whether . . . that of a professional man or of any other person."<sup>58</sup>

Note these three features of goodwill at common law as it solidified in the mid-nineteenth century: (1) It attaches always to a business, never to a person—not even to a professional person. (2) Lindley is contemplating the sale of a *thing*, the goodwill of the business, and not a sale of any *personal characteristic of the seller* of that business. (3) The value of the goodwill does not depend in any way upon some enhanced value over and above what the purchased

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55. *Ballero v. Heslin*, 128 So. 2d 453, 455 (La. 4th Cir. 1961).

56. *Morgan v. Perhamus*, 36 Ohio St. 517, 524 (Ohio 1881).

57. *Id.* at 523 (emphasis added).

58. *Id.* at 522 (emphasis added) (quoting Lindley, *A Treatise on the Law of Partnership* (1860)). In addition, Lindley provides here yet another instance of an old legal document eerily casting a shadow across a modern dispute. Notice how clearly Lindley anticipated the "excess profits" issue in his brief paragraph when he drew a distinction between "keeping a connection" and "improving a connection." Over 140 years later, accountants and lawyers can be found still wrestling over whether or not "increased profits" are a part of goodwill. Compare Lindley's "keeping" versus "improving" profits distinction with the Parkman-Zipp-Levis discussion of "increased profits" versus "excess profits." See *infra* Part II.C.1.

business should “normally” earn. For Lindley, a buyer is getting an opportunity to do better, not an expectation, much less any *entitlement*, to do better.<sup>59</sup> Baron Lindley was hardly alone in this view. Parsons, in at least the fourth edition of his treatise, characterized the rate of return from the purchase of goodwill as “a hope or expectation, which may be reasonable and strong . . . but it is, after all, nothing more than a hope, grounded upon a probability.”<sup>60</sup>

The Louisiana Supreme Court reached the identical conclusion in 1947 that the Ohio Supreme Court had reached in 1881: “[absent] an expressed stipulation to the contrary in the contract, the sale of the good will of the business did not preclude [a defendant] from engaging in a similar undertaking in [the same town] . . . or elsewhere.”<sup>61</sup> Moreover, in *Dantonio v. Fontana*, the Louisiana Supreme Court confirmed *Davis v. Dees*.<sup>62</sup> Also of interest is *dictum* that the “[s]ale of a business and its good will does not preclude the seller from competing in a similar business, not even shortly thereafter and in the immediate vicinity.”<sup>63</sup> The court then cited *Bergamini v. Bastian*, summarizing its holding as “‘in the absence of an express stipulation . . . a contract in restraint of trade cannot be presumed and enforced by the courts,’ citing American and French authorities.”<sup>64</sup> Additionally, the 1994 *Dantonio* Court found it useful to note that the 1883 *Bergamini* opinion had relied upon “Justice Story’s much quoted, often paraphrased definition of good will,” which the 1883 panel had quoted in full.<sup>65</sup>

The common law has had some subtle shifts in the legal definition of goodwill despite the great overall stability of the term. The third and last of the oft quoted definitions is by Justice Cardozo from a case remarkably like *Smith v. Everett*. *In re Brown* also involved a widow who believed the surviving partners had not properly accounted for business good will (this time in a stock brokerage).<sup>66</sup> After noting that “books abound in definitions of good will” so that “[t]here is no occasion to repeat them,” Judge Cardozo observed that “any privilege that gives a reasonable expectancy of preference in the

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59. Lindley’s *A Treatise on the Law of Partnership*, although first published in 1860, is not some obscure, obsolete treatise. The eighteenth edition, *Lindley on the Law of Partnership*, reaching 1131 pages of text, was published in 2002 by Sweet and Maxwell in London. See Lindley on the Law of Partnership (Roderick C. L’Anson Banks ed., 18th ed. 2002). Baron Lindley, 1828–1921, entered the bar in 1850 and had a distinguished legal career before finally retiring in 1905.

60. Parsons, *supra* note 41, at 239.

61. *Davis v. Dees*, 211 La. 229, 232, 29 So. 2d 774, 776 (1947).

62. *Dantonio v. Fontana*, 92-2844 (La. 1994), 636 So. 2d 218, 225.

63. *Id.* at 224.

64. *Id.* at 224–25.

65. *Id.* at 225 n.19.

66. *In re Brown*, 150 N.E. 581 (N.Y. Ct. App. 1926).

race of competition" will be bought, whether "such expectancy ... [is due to] . . . place or name or otherwise" of a "business that has won the favor of its customers."<sup>67</sup> This "expectancy" ranges from "so strong . . . [it] may be said to be a certainty" to "so weak that for any rational mind they may be said to be illusory."<sup>68</sup>

Many of the ancillary concepts examined in *Smith* were also reviewed, without change, in *Brown*, such as the surviving partners' right to remain in the brokerage business despite having liquidated the partnership.<sup>69</sup> For present purposes, however, the key fact of *Brown*, regardless of the added factors used to generate good will ("place or name or otherwise"), is that none of them were called out as a personal characteristic of any individual.<sup>70</sup> Even in Cardozo's—only very slightly—expanded concept, goodwill is still solely a characteristic of a business and not of a person.

Cardozo also clearly appreciated the wide range of variation in the likelihood of some return from the goodwill purchased with a business.<sup>71</sup> For Cardozo, the future return from goodwill can legitimately be either a chance or a virtual guarantee. However, the "rate of return's" size has no legal significance—both "certainty" and "illusion" will still qualify as goodwill. Both flow from a business; neither flows from any personal quality of the seller. Cardozo is not excusing fraud when he speaks of "illusion." He is merely noting how greatly valuation differences can be to "rational minds."

### *C. Broadening of the Goodwill Concept: Multiple Meanings in One Term*

As has been shown in Part II. B., the legal concept of goodwill, as used and understood within the discipline of law, has been remarkably stable for at least 160 years, and perhaps for almost 200 years, depending upon how alike one chooses to consider Lord Eldon's view in *Cruttwell* and Justice Story's definition in his partnership treatise.<sup>72</sup> Of course, any rule can operate consistently

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67. *Id.* at 582. One case Justice Cardozo cited as containing a "book" of good will definitions was *People ex rel. A. J. Johnson Co. v. Roberts*, 53 N.E. 685 (N.Y. Ct. App. 1899). *Id.* That case began with *Cruttwell*, included a different quote from Sir John Romilly, and then carried Lindley's definition forward to the 1895 edition of his *Partnership*. *Roberts*, 53 N.E. at 688–89.

68. *Brown*, 150 N.E. at 582.

69. *Id.*

70. *Roberts*, 53 N.E. at 688–89 (citing Lindley, *supra* note 59).

71. The "certainty-to-illusion" spectrum of a case like *In re Brown* is treated later as the "excess value" question. See *infra* part II.C.1.

72. Of course a famous case draws commentary when cited in an appeal. An 1899 Illinois First Circuit case quotes an 1896 English case arguing that Lord Eldon's definition is "too narrow," as follows:

only when judges are confident that “the rule” is settled and further that “the rule” applies to the case at bar. For example, a very late nineteenth-century Illinois Court of Appeal opinion approvingly quoted Lindley’s belief that “[t]he term ‘goodwill’ can hardly be said to have any precise signification. It is generally used to denote the benefit arising from connection and reputation.”<sup>73</sup>

“Goodwill,” outside of law, is unfortunately still not well settled almost 200 years after an English judge first laid down its parameters within a courtroom. Numerous articles and cases illustrate that the component parts of goodwill derived from accounting and economics vary from case to case, as well as between equity matters and other areas of the law, such as federal taxation in the United States. For example, Alan S. Zipp, an attorney and a certified public accountant (CPA), did not attempt a modern definition, concluding instead after a survey of his two fields that “[g]oodwill is a mysterious possession, elud[ing] precise definition, . . . [and, although all] experts agree it exists, few experts agree on exactly what it is . . . [Many] have tried

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If the language of Lord Eldon is to be taken as a definition of good will of general application, I think it is far too narrow, and I am not satisfied that it was intended by Lord Eldon as an exhaustive definition. Good will must mean every advantage—every positive advantage, if I may so express it—as contrasted with the negative advantage of the late partner not to carry on the business himself, that has been acquired by the old firm in carrying on its business, whether connected with the premises in which the business was previously carried on, or with the name of the late firm, or with any other matter carrying with it the benefit of the business; and it is absurd to say that when a large wholesale business is conducted the public are mindful whether it is carried on in Fleet street or in the Strand.

Douthart v. Logan, 86 Ill. App. 294 (Ill. App. Ct. 1st Cir. 1899) (quoting *Trego v. Hunt*, Law Reports, Appeal Cases 1896, 17). The treatment of goodwill by surviving partners and the conditions under which they might carry on the business is an issue beyond the scope of this comment, although such points are extensively covered in both the Story and Parsons treatises. See Story, *supra* note 38; Parsons, *supra* note 41.

73. *Id.* at 309. Interestingly, despite the lack of precision inherent in the term “goodwill,” the Illinois Supreme Court not only affirmed every holding but thought “[i]t would be interesting to consider the question as a legal one, so fully argued by counsel, whether or not the business was of such a character as that, independent of contract, there would be a good will belonging to the partnership.” However, upon review of the record, the court was

satisfied . . . there was no good will as an asset of the firm, and that it was intended by the co-partners that there should be none. It cannot be doubted that it would have been competent for the partners to contract with each other that there should be no good will, to be considered as property or as an asset of the co-partnership. Such a contract might be expressly made, or it might arise by implication from other contracts and the acts and conduct of the parties in interest.

Douthart v. Logan, 60 N.E. 507, 510 (Ill. 1901).

[to define and value it] but [t]he most striking characteristic of this immense amount of writing is the number and variety of disagreements reached."<sup>74</sup> Yet another modern take on goodwill is from the International Glossary of Business Valuation Terms. Robert W. Levis cited that definition as "that intangible asset arising as a result of name, reputation, customer loyalty, location, products, and similar factors not separately identified."<sup>75</sup>

A leading indicator of the sometimes very subtle but still profound shifting in meaning of the term "goodwill" occurring over the last few decades is found in the current definition of goodwill in *Black's Law Dictionary*. Lord Eldon might have recognized the first half of this definition; Justice Story surely would have. *Black's* initially focuses on a "business's reputation, patronage, and other intangible assets . . . considered when appraising the business, esp. for purchase" but then adds "the ability to earn income in excess of the income that would be expected from the business viewed as a mere collection of assets."<sup>76</sup>

However, the second half of *Black's* definition, the "excess income" notion, is solely based upon economic considerations and cannot be found in the line of cases stretching from *Cruttwell* through *Smith, Morgan*, and *Bergamini* to *Dantonio*. Of course no one can know what Lord Eldon or Justice Story would have made of the "excess income" approach.<sup>77</sup> However, one may nonetheless fairly conclude even an extraordinarily skilled advocate would be hard pressed indeed to extract the "excess income" concept from within the *Cruttwell-Dantonio* line.

The *Black's* definition for goodwill, immediately after the "reputation" and "excess" language, refers to a new term, "going concern value." The definition further defines "going concern value," in pertinent part, as "the future earning power" of a business, "as opposed to the liquidation value of the business or its assets. Going-concern value includes, for example, goodwill."<sup>78</sup> That goodwill is

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74. Alan S. Zipp, *Divorce Valuations of Business Interests: A Capitalization of Earnings Approach*, 23 Fam. L.Q. 89, 95 (1989) (citing J. Canning, *The Economics of Accountancy* 38 (1929)).

75. Levis, *supra* note 24 (citing *The International Glossary of Business Valuation Terms*).

76. *Black's Law Dictionary* 703 (7th ed. 1999). Zipp cited an earlier edition of *Black's*: "the ability of a business to generate income in excess of a normal rate on assets due to superior managerial skills, market position, new product technology, etc. In the purchase of a business, goodwill represents the difference between the purchase price and the value of the net assets." Zipp, *supra* note 74, at 95 (citing *Black's Law Dictionary* 625 (5th ed. 1979)).

77. In fact, there is still some measure of conflict today between accounting and law as to what "excess" actually means. See *infra* Part II.C.1.

78. *Black's Law Dictionary* 1549 (7th ed. 1999).

so closely bound up with its corresponding business entity that it cannot be had apart from that business is unremarkable.<sup>79</sup> However, the *Black's* concept of goodwill goes a step further, subsuming goodwill within still another concept, "going concern."<sup>80</sup> Additionally, cases occasionally co-mingle these two concepts.<sup>81</sup>

### 1. Accounting and Economic Views of Goodwill

As Allen Parkman noted, economics explains why goodwill exists, while accounting measures its value. These economics and accounting concepts might distinguish business and personal goodwill of professional practices, influencing how they should be treated in property divisions.<sup>82</sup> This "distinguishing" task is highly problematic, since "what the courts is [sic] treating in many cases as professional goodwill is just personal goodwill based upon the individual's reputation."<sup>83</sup>

So, "[f]rom an economic perspective, goodwill is an asset, whose value—as with all other assets—depends upon the future returns it will generate. . . . The economic concept of goodwill is introduced when the future revenues of an organization cannot be assigned to the contribution of a finite list of assets. . . . [It] is

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79. See, e.g., *Vonderbank v. Schmidt*, 44 La. Ann. 264, 266–69, 10 So. 616, 617–18 (1892). Numerous other cases over the last 150 years hold that goodwill cannot be acquired separately from a business entity.

80. For a more detailed examination of the mixing of "goodwill" with "going concern," especially in tax matters, see *infra* Part II.C.2.

81. Goodwill was held to be a component part of a going concern in *Gaydos v. Gaydos*, 693 A.2d 1368, 1375 (Pa. Super. Ct. 1997). However, that case was also remanded with instructions to deduct the professional goodwill of the husband's dental practice from the marital estate. *Id.* The *Gaydos* court "in no way wish[ed] to add to the confusion in this area of law, and recognizing the trial court's best efforts in resolving this confusion . . . [but] suspect[ed] that much of what the trial court considered going-concern value was actually professional goodwill." *Id.* But, the *Gaydos* opinion also stated that "[g]oodwill is, therefore, one benefit among many of owning a fully-functional business rather than a collection of assets. It follows that goodwill value is a *component* of the going concern value of a business; goodwill and going concern are not 'separate methods' of valuing the same intangible thing." *Id.* (emphasis in original). It is therefore an open question whether *Gaydos* adds or subtracts from the legal confusion about personal goodwill in divorces.

82. Parkman, *A Systematic Approach*, *supra* note 24, at 1. Of course, the central dispute in such cases as *Ellington* is whether business and personal goodwill should be distinguished. "[I]t is difficult to adapt the standard method for calculating business goodwill in an on going enterprise to *individuals*." *Id.* at 10 (emphasis added). Well, yes . . . exactly!

83. *Id.* at 11.



created by the standard economic method of investing current resources to increase future profits."<sup>84</sup> By contrast, "[t]he general guides for thinking about accounting goodwill are: (1) a payment in excess of an established value of a resource and (2) enhanced earning power."<sup>85</sup> Since many other intangibles can increase the value of a business (patents, trademarks, and leaseholds), "their value is frequently attributed to goodwill."<sup>86</sup>

Zipp's conclusion from the perspectives of both accounting and law is a remarkable point of view. He believes "[t]here is no substantive difference between commercial goodwill and professional goodwill from either a legal or an economic perspective" since both just "represent the value of a going business" above the value of "the underlying tangible assets."<sup>87</sup> So, in his view, "marital property rules treat [both types of] these businesses as valuable property rights which must be considered in making equitable distributions and monetary awards."<sup>88</sup>

At least three important concepts warranting close examination are tightly packed into Zipp's few lines. First, these statements are true only if one assumes that some personal attribute of an individual can be a thing owned by more than one person. Second, they deal with the "excess" concept as solely the difference between the return from the mere tangible assets of a business versus the return from the entire business. Third, they assume that professional goodwill is a business.<sup>89</sup>

Moreover, there is some dispute as to the meaning of "excess value." Parkman sees both "greater profits" and "increased future profits" as features of business goodwill.<sup>90</sup> On the other hand, Levis, a Colorado CPA, sees "excess" as Zipp does, meaning a rate of return higher than the market rate "over a 'reasonable, fair

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84. *Id.* at 6-8.

85. *Id.* at 8.

86. *Id.* at 8-9.

87. Zipp, *supra* note 74, at 102.

88. *Id.*

89. A key goal of Parkman's was to "analyz[e] the difference between the business goodwill of the professional enterprise and the personal goodwill of the professional individual." Parkman, *A Systematic Approach*, *supra* note 24, at 1. "It is important to realize that goodwill is an asset of the business, not of any individual." *Id.* at 8. This accounting and economics subpart only reviews the second concept, "excess value." For coverage of the other points, see the clientele-goodwill summary *infra* Part III.A.

90. *Id.* at 8. This is because, if "a business is more profitable than its competitors because of the superior abilities or business connections of an individual, . . . the profits of the firm will return to a normal level and any enhanced profits will disappear" if that key person leaves. *Id.* For Parkman, goodwill thus both attaches only to the business and also explains higher than normal profits.

market compensation.”<sup>91</sup> Levis refers to any “excess” compensation as “part of the ‘income normalization’ process.”<sup>92</sup>

The accountants thus have several methods for calculating goodwill but no plain definition of it. In Parkman’s view, “[t]he general feeling is that verbal descriptions of goodwill are inadequate and that the only way to measure what is meant by goodwill is to observe the way that it is measured.”<sup>93</sup> The economists have various explanations for the existence of value in a company over and above the tangible assets of the firm but they leave the calculating of its value to the accountants.<sup>94</sup>

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91. Levis, *supra* note 24, at 74.

92. *Id.*

93. Parkman, *A Systematic Approach*, *supra* note 24, at 8. Parkman was writing in 1998, so the controlling directive for goodwill was still Accounting Principles Board Opinion 17 (APB 17), “Intangibles,” issued in August 1970. As he said in 1998, “Goodwill is not defined in Accounting Principles Board Opinion 17, but the measurement process, deductive in nature, is described.” *Id.* at 8 n.45. However, beginning with fiscal years starting after December 15, 2001, the June 2001 Statement of Financial Accounting Standards no. 142 (SFAS 142), “Goodwill and Other Intangible Assets,” superceded APB 17. See Statement of Financial Accounting Standards no. 142, Introduction. SFAS no. 142 defines goodwill as

The excess of the cost of an acquired entity over the net of the amounts assigned to assets acquired and liabilities assumed. The amount recognized as goodwill includes acquired intangible assets that do not meet the criteria in FASB Statement No. 141, Business Combinations, for recognition as an asset apart from goodwill.

*Id.* no. 142, appendix F. SFAS no. 141 is primarily noted within the financial community for substituting the “purchase” method for the “pooling” method in mergers and acquisitions. See *id.* no. 141. A typical characterization of the effect of these two new financial policy statements is made by Caliber Advisors, Inc.:

Caliber regularly advises public and private companies on the value of intangible assets, their economic lives and levels of impairment. Recent accounting rule changes require companies to:

1. Provide much more detailed information about intangible assets and purchase allocations.
2. Regularly review the value of these intangible assets for impairment, including goodwill.

In 2001, the Financial Accounting Standards Board (FASB) approved two new statements (141 and 142) to redefine the ways in which firms report acquisitions. Statement 141 eliminated the ability to use pooling-of-interest accounting, which allowed firms to protect their reported earnings from acquisition amortization expenses. Statement 142 rule eliminated the need to amortize goodwill, and instead established standards for evaluating goodwill impairment on an annual basis.

Caliber Advisors, Inc., *SEC Reporting: SFAS 141 and 142 Engagements*, at [http://www.caliberadvisors.com/news\\_sf141and142.htm](http://www.caliberadvisors.com/news_sf141and142.htm).

94. Parkman, *A Systematic Approach*, *supra* note 24, at 2.

## 2. Importation of "Going Concern" Into "Goodwill"

Some authorities do continue to maintain the distinction between these two concepts. For example, the Pennsylvania Supreme Court still recognizes them to be different, and "technically distinct," with "going concern" meaning "the ability of a business to generate income without interruption [despite a] change in ownership" while goodwill is the more like the traditional "preexisting relationship arising from a continuous course of business which is expected to continue indefinitely."<sup>95</sup> However, any close examination of the relationship between "going concern" and "goodwill" must inevitably lead into the Internal Revenue Code, in which Congress has chosen to puree goodwill with going concern.<sup>96</sup>

Whether by accident or design, Congress firmly mixed and mated what should be two distinct concepts in its income tax statute. Section 197(d)(1)(A) of the Internal Revenue Code includes "goodwill," without defining it, in a list of things which includes, *inter alia*, the terms "going concern" and "workforce."<sup>97</sup> These listed factors require consistent tax treatment. Slightly further along in the tax laws, one comes to section 197(f)(1)(B), a "Special rule for covenants not to compete," which provides that no such covenant (by which Congress means any "other arrangement" to that effect), "may be treated as disposed of (or becoming worthless) before the disposition of the entire [business] interest described . . . [in the non-compete agreement]."<sup>98</sup> Again, that goodwill can have no

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95. *Butler v. Butler*, 663 A.2d 148, 152 (Pa. 1995). Even here, however, notice that the definition of goodwill has shifted in emphasis away from pure law and towards economics. *Cruttwell's* "probability," in the sense of "the chance the old customers will still come," has gone from a "preexisting relationship" (old customers remaining with the new firm) to become a "continue indefinitely" expectation, rather more like a guarantee than a chance. On the other hand, Pennsylvania does not presume that goodwill must reflect a "course of business" that is more profitable than the "usual" rate of return. "Excess" in that sense is absent here. One is reminded of the comment supposedly made by the one term New York Mayor Abe Beame, circa 1975; words to the effect that he would not rest until every resident of the city had an "above average" income.

96. The tax code impinges upon goodwill in divorce actions in at least one other way. The "willing buyer, willing seller" formulation plays a role in calculating goodwill. See 26 C.F.R. § 25.2512-1 (2002). While useful in valuing a community business being sold to an outsider, the formulation is of little help in divorces. *Ellington v. Ellington*, 36,943 (La. App. 2d Cir. 2003), 842 So. 2d 1160, 1167.

97. I.R.C. § 197(d)(1)(A) (2002).

98. *Id.* § 197(f)(1)(B).

independent existence apart from a business is universal Black Letter law.<sup>99</sup>

Moreover, the implementing Treasury Department regulation places both “goodwill” and “going concern” into the same paragraph and refers to another paragraph as to whether the goodwill does or does not “attach to the assets.”<sup>100</sup> The tax regulations do not finally define these two terms, “goodwill” and “going concern,” until yet another paragraph.<sup>101</sup> The first is given as the “expectancy of continued customer patronage.” This falls strictly in line with two centuries of the classic common law understanding of the term “goodwill.” The second definition, for a “going concern,” is “the additional value that attaches to property because of its existence as an integral part of an ongoing business activity.” Two things should be immediately apparent. First, the Internal Revenue Service (IRS) is explicitly attempting to correct an error made by Congress by separating “goodwill” and “going concern” back into two distinct things. Second, the IRS presumes that the income stream from the concern being sold will not be interrupted by the change in ownership.

Restoring this distinction is to the credit of the IRS. There need not be any connection or linkage whatsoever between any personal quality of a firm's present owners (such as reputation, skill, knowledge, or work ethic) and an interrupted future income stream. For example, there are closely held family businesses owning vast tracts of land (6,400 acres—ten square miles—in a single plot) in Louisiana with one hundred year timber leases from major lumber and paper concerns. Should these families ever elect to sell their firms, any new buyer would be as assured as anyone can ever be of a reliable future income stream. Moreover, no part of the value of the remaining forty-six years (of a one hundred year lease signed in 1949) of timber operations bears any relationship even to the business acumen of the leasing firms. Unless and until people stop having babies and living in homes, the *Pinus taeda* (a variety of pine tree commonly harvested for lumber) will continue to become two-by-fours.

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99. Moreover, nothing mandates that every business has goodwill. There are abundant cases involving media outlets holding that people do not listen to a radio station or watch a television station because of its owners or its management. Customers tune to the programs, not to a station. Whatever goodwill is present attaches to the personalities on the air and not to the personalities in the front office or to the station itself. See *KFOX, Inc. v. United States*, 510 F.2d 1365, 1377 (1975); *Meredith Broad. Co. v. United States*, 405 F.2d 1214, 1216 (1971).

100. 26 C.F.R. §§ 1.197-2(e)(1), 1.1060-1(b)(2) (2002).

101. *Id.* § 1.1060-1(b)(2)(B)(ii).

Finally, the United States Supreme Court has joined the periodic grappling with the concept of goodwill a time or two, usually in tax cases. *Newark Morning Ledger Co. v. United States* contains a useful, tightly bundled thumbnail of several of these concepts.<sup>102</sup> *Morning Ledger* cites *Metropolitan Bank's* "consider[ing] whether a newspaper's goodwill survived after it was purchased and ceased publishing under its old name."<sup>103</sup> *Metropolitan*, "relying on Justice Story's notable description of 'goodwill,'" concluded goodwill "did not survive" such a sale.<sup>104</sup> The other cases *Morning Ledger* followed were *Des Moines Gas* (goodwill is "that element of value which inheres in the fixed and favorable consideration of customers, arising from an established and well-known and well-conducted business")<sup>105</sup> and *Los Angeles Gas* ("going concern" is not the same thing as "good will" in computing "rates for public utilities").<sup>106</sup>

Everyone has heard the phrase "a difference in degree, not in kind." *Morning Ledger* illustrates that distinction perfectly. This tax case turned on deductibility versus amortization of the goodwill represented by subscriber lists after a merger of two newspaper companies.<sup>107</sup> In a pure business context, involving only the straightforward application of accounting principles and the tax code, the mixing of law, accounting, and economics in this fairly complicated goodwill tax issue resulted in a simple, although controversial, outcome—the newspaper was allowed the deduction.<sup>108</sup>

However, attempting to blend these same accounting and economics principles into divorce settlements is not a matter of degree. It is a difference in kind. People are not businesses. Personal

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102. 507 U.S. 546, 113 S. Ct. 1670 (1993).

103. *Id.* at 555 (citing *Metropolitan Bank v. St. Louis Dispatch Co.*, 149 U.S. 436, 13 S. Ct. 944 (1893)).

104. *Metropolitan Bank*, 149 U.S. at 446, 13 S. Ct. at 948 (citing Story, *supra* note 39, § 99). Note that the Justice Story text quoted in *Metropolitan Bank* was his first formulation covering ordinary *commercial* partnerships and not the second one on *professional* partnerships.

105. *Des Moines Gas Co. v. Des Moines*, 238 U.S. 153, 165, 35 S. Ct. 811, 814 (1915).

106. *Los Angeles Gas & Electric Corp. v. Railroad Comm'n of California*, 289 U.S. 287, 313, 53 S. Ct. 637, 647 (1933).

107. *Morning Ledger*, 507 U.S. at 550–51, 113 S. Ct. at 1672–1673.

108. *Id.* at 572, 113 S. Ct. at 1683. *Morning Ledger* was a 5–4 decision. Justice Souter's dissent quoted both Lord Eldon's *Cruttwell* opinion, originating the legal definition of goodwill, as well as Justice Story's classic definition. Significantly, Justice Souter followed *Metropolitan's* use of Story's first formulation (for ordinary *commercial* partnerships) and not the second one (for *professional* partnerships). Joining in the dissent were both Chief Justice Rehnquist and Justice Scalia, an unusual alignment to say the least. Congress created section 197 of the Internal Revenue Code in response to *Morning Ledger*. See Pub. L. No. 103–66, 107 Stat. 312.

characteristics are not assets. The sort of dispute involved in *Morning Ledger* is not simply “more difficult” or “less certain” when transferred into the realm of some particular person's knowledge, skills, effort, or reputation. The problem is not that the accounting razor is too thick or too dull when used on personal goodwill in lieu of business goodwill. The problem lies in making the attempt at all. The problem lies in attempting to cut something that is not there. The problem lies in treating the personal attributes of a human being as a divisible community asset. The next part of the comment begins analysis of the practical difficulties flowing from the attempt to value people as businesses.

*D. Goodwill as Currently Employed Within Common Law Divorce Litigation*

*1. The Present “Two Source, Two Effect” Concept*

Numerous experts have attempted to provide guidance to practitioners on the sources, nature, differences, and similarities of various types of goodwill as it affects partitions. Kalcheim's thoughts are typical of that effort, noting that valuator's often attempt to measure “personal goodwill using accepted methodology even when no enterprise goodwill exists” because it is so difficult to factor out “personal goodwill from enterprise goodwill, particularly where one spouse is involved in a professional service business such as a medical, dental, accounting, or law practice.”<sup>109</sup> The problem “is not limited to service businesses” since “any business where the earnings are largely due to the spouse's personal efforts poses this problem,” such as “insurance agencies and construction companies.”<sup>110</sup> In his opinion, “[t]he confusion in the courtroom arises less in the law than in the proofs. Personal and enterprise goodwill may or may not appear to be mutually exclusive.”<sup>111</sup>

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109. Kalcheim, *supra* note 22. Another way to cast the thesis of this comment could be, “Do not use accepted methodology to calculate the value of a thing that cannot be sold, traded, or transferred, such as an attribute of someone's personality.”

110. *Id.*

111. *Id.* Still another way of stating the thesis of this comment could be, “Personal and enterprise goodwill *must always be mutually exclusive*.” Similarly, Parkman has argued that Kalcheim's “confusion in the courtroom” was induced by importing an accounting concept of the same name but with a different meaning into the legal arena. For example, he highlights *In re the Marriage of Lukens*, 558 P. 2d 279 (1976), as a good “illustrat[ion of] the problems when the courts recognize a concept from another field, in this case goodwill, and then establish an inappropriate method for its valuation.” Parkman, *A Systematic Approach*, *supra* note 24, at 6 n.38.

Another authority, Robert W. Levis of Colorado, endeavoring to provide guidance to lawyers attempting to sort out how the varieties of goodwill affect a partition, writes that "differences in assigning value [for goodwill] . . . usually relate primarily or exclusively to the difference between 'enterprise goodwill' and/or 'professional goodwill.'" <sup>112</sup> The former is "the intangible value . . . associated primarily with the business as an institutional entity," while the latter is "the intangible value . . . associated primarily with the individual practitioner or owner/operator of the business." <sup>113</sup> While Levis cautions that this "distinction between enterprise goodwill and personal goodwill is not always clear," it is necessary for "a well-performed valuation analysis" because, in his home state of Colorado, both "are considered property." <sup>114</sup>

The valuator's problem in weighing a business value that "transcends the individual owner or practitioner," has a "different risk profile," has a "different value" from "the same level of expected income," and may or may not be "associated exclusively with the individual owner of the business" is "one of the most challenging tasks associated with appraising business interests." <sup>115</sup> Therefore, "[t]he business valuator . . . should attempt to identify whether income is being generated *by the entity* or *by the individual*." <sup>116</sup> Levis notes that this "separation" difficulty (the value of enterprise goodwill minus the value of any personal goodwill) "is not unique to marital dissolution proceedings" since it must also be done in an ordinary sale of a business. <sup>117</sup> However, this valuation process "is more difficult" for a divorce than in a sale because "a cash equivalent value opinion must be the end result," yet a divorce is quite "[u]nlike an acquisition transaction, [where] the business's value can . . . be conveyed via structure and contracts." <sup>118</sup>

Tracing the first source-effect pair, "enterprise-commercial" goodwill, reveals that it attaches to the business itself and is an integral part of it. Enterprise goodwill is thus an inextricable feature of what a civilian would say is a separate juridical person, an "artificial person;" what the French would call a "moral person." <sup>119</sup>

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112. Levis, *supra* note 24.

113. *Id.*

114. *Id.*

115. *Id.*

116. *Id.* (emphasis added).

117. *Id.*

118. *Id.* Of course, if the income is being generated by the *individual* rather than by the *entity*, how can anything but a human being be the object of valuation here?

119. Boris Starck, *Droit Civil: Introduction*, no. 166, at 74 (1976) (J.R. Trahan trans. 1997).

"Enterprise" goodwill is thus the source of "commercial" goodwill. However, the better analysis would be that they are but two different names for the same concept. Consider how one common law practitioner sees the interaction between "enterprise goodwill" and "personal goodwill." Randall B. Wilhite argues that goodwill of a business "ascribable only to an individual owner," especially to one who "is selling (and leaving the business)," is "almost never part of the compensation paid by the buyer" for the business.<sup>120</sup> Anytime there is a turnover of personnel, "there is no assurance that the continued goodwill of a business will continue" because, regardless of "individual work effort," the true factor is whether the good will "can be transferred as an asset of the business rather than the individual."<sup>121</sup>

Wilhite went on to observe that "[m]any courts around the country draw a line between various components of goodwill" because any value from "personal goodwill . . . will be realized, if at all, only with post-divorce efforts of that person," while "entity [business/commercial/ enterprise] goodwill is divisible as an asset of the marriage . . . because it is [not] particularly germane to the persona of the individual" selling the business.<sup>122</sup>

Three things stand out in Wilhite's modern commentary on the relationship between "enterprise" (or business/commercial) and "personal" goodwill that could have been written by Lindley, Parsons, Eldon, or Romilly: (1) personal goodwill is not a "thing," not "property," such that it can be sold; (2) the "sale" of personal goodwill is actually a "non-compete" agreement; and (3) marketable goodwill is only the expectation of repeat business to the new owner from customers of the old owner. Nonetheless, despite this sound doctrinal beginning, Wilhite then elects to blur the vitally important difference between value attached to a business and value attached to a person as follows, "In this article, *no distinction is made between professional goodwill and personal goodwill*, and further, all personal goodwill will be that goodwill, if any, in a business that is related to one or both of the divorcing spouses, and not any other individual employees in the business."<sup>123</sup> From that premise, the inevitable result can only be the valuation of a human being, not of the business he or she owns.

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120. Randall B. Wilhite, *The Effect of Goodwill in Determining the Value of a Business in a Divorce*, 35 Fam. L.Q. 351, 354 (2001).

121. *Id.* at 355.

122. *Id.* at 358-59.

123. *Id.* at 359 n.24 (emphasis added).



2. *The Cumulative Impact of Accounting and Economics on Marital Property Concepts*

Goodwill as a legal concept arose purely in a business context and the legal understanding of it has worked quite well in the business arena for nearly 200 years. Perhaps a second year law student ought to pause before challenging as venerable and as established an institution as *Black's Law Dictionary* . . . but . . . its two entries, "goodwill" and "going concern," are poorly drafted. However, the slow but significant falling away from the original legal concept underpinning goodwill so evident in *Black's* today is more of a symptom than a problem. It is simply another reflection of the damage and confusion created in law by importing accounting and economics concepts with the same name as important legal concepts but with quite different meanings.<sup>124</sup> As Alan M. Parkman so well observed, "[i]n no area is this ad hoc approach [of assessing goodwill] more visible than the courts' consideration of the goodwill of professional practices. Th[ese] . . . dispute[s] in property settlements at divorce" are due to a "lack of an understanding of what is goodwill, how it is created and how it should be valued."<sup>125</sup>

Even doctrinal works of law have been adversely affected by imported accounting principles. The Spaht and Hargrave treatise contains an examination of the "commercial-professional" goodwill problem that displays a position incompatible with civilian doctrine. Their analysis of the treatment of a consulting engineering firm in a partition turns on the "underlying reason for excluding good will in the valuation of some professional practices" being "essentially capitalization of future earnings" such that "separate future earnings [should not] be treated as present community property."<sup>126</sup> For them, the dispositive factor is "whether the good will value represents future earnings or not."<sup>127</sup>

The better reason to exclude personal goodwill is that no personal attribute can be owned by two people. An individual's personality must always be separate property, to the extent that it can ever be property at all. Their treatise rejoins sound civilian doctrine a few lines later, holding that such a case should focus on "whether the [professional] corporation had value and could continue to produce income even without the efforts of the former husband." This fact based inquiry would focus on the capabilities of the three other

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124. See *supra* note 111.

125. Parkman, *A Systematic Approach*, *supra* note 24, at 1.

126. Spaht & Hargrave, *supra* note 15, § 2.8, p.5 (Supp. 2002) (examining *Collier v. Collier*, 790 So. 2d 759 (La. App. 3d Cir.), writ denied, 803 So.2d 30 (2001)).

127. *Id.*

employees and the likelihood of their being able to produce business and profits without the principal.<sup>128</sup>

Goodwill arose in the pure business context and the legal understanding of it has worked quite well in that business arena for nearly 200 years. The whole problem with goodwill in divorces arose when the urge to "collectivize" the income generation capability of a couple collided with the centuries old legal principle that a community property regime terminates at divorce.<sup>129</sup> It thus became necessary to modify (or "distort," depending upon one's point of view) the definition of goodwill sufficiently so that it could apply to a characteristic or quality of a person instead of only attaching to a business.

Frantz and Dagan argue that half of all future income (traceable to any origin whatsoever within the duration of the marriage), from whatever source derived, goes to the ex-spouse.<sup>130</sup> They are not concerned with professions, businesses, goodwill, or any other breakdown by category. If income to the ex-spouse had any origin, however slight, from within the marriage, it is divisible community property.<sup>131</sup> That some portion of this income is generated by any personality feature of the ex-spouse or that it will not be earned until after the divorce is, to them, irrelevant. The ex-spouse acquired the ability to earn income during the marriage so that ability is itself community property. The proceeds of this asset-earning ability of community's are therefore divisible without regard to when they accrue or are received.<sup>132</sup> This amounts to shifting the future earnings of an ex-spouse back into the community by characterizing them as some sort of current marital asset.

The concurring opinion from *Chandler* in Idaho is critical to understanding the adverse effects within family law of the application of the business concept of goodwill to people: "A spouse's knowledge, background, talents, abilities . . . and so forth are not community property . . . [they are] separate property. Discounting estimated post-divorce income to a present value *does not convert it*

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128. *Id.*

129. Frantz & Dagan, *supra* note 23, at 110. Frantz and Dagan's use of "collectivize" offers a splendid opportunity for iconoclastic feminist legal scholarship: construction of a legal rationale that simultaneously undercuts the sexual objectification of women while supporting the objectification of ex-spouses as a feature of the businesses they own or the professions they practice.

130. *Id.* at 107.

131. *Id.* at 108.

132. *Id.*

into community property.”<sup>133</sup> Three key points flow from these two lines in *Chandler*.

First, the essence, albeit unarticulated, of the “personal goodwill” position is that the community never ends. Frantz and Dagan explicitly want half of all future income dedicated to the ex-spouse even if those dollars are not earned until after the divorce. “[Division of] a spouse’s future earning potential gained during marriage . . . should extend to [all] future earning potential generated during the time of marriage, however derived.”<sup>134</sup> This isn’t because there is some accounting reason, or some economic rationale, to “correctly value” a restaurant (or a medical practice, a book of contacts, or a legal practice, etc.) as of the divorce. Instead, a policy choice, a value judgment, has been made. As they phrase it, “[a] commitment to the ideal of marriage as an egalitarian liberal community requires treating spouse’ increased earning capacity as marital property . . . [;] this proposal may be the most important reform we recommend.”<sup>135</sup> This is a “results oriented” shoe horn at work. Nothing in accounting or economics dictates any particular disposition of the future income of a divorced doctor or cotton broker. Nor is either accounting or economics cited to justify the policy.

Second, the laws of forty-nine of the fifty states must be changed to make this capture of “future earning potential” possible, since “[c]urrently, most jurisdictions refuse to include increased earning capacity within the marital estate. In fact, only New York has a clearly established rule making at least some of this asset—professional degrees obtained during marriage—eligible for division.”<sup>136</sup> Since the community supposedly terminates in a divorce, all income from restaurant, legal or medical practice, carpet-laying, or cotton-brokering operations must stop falling into the community once the community terminates. The challenge is to somehow divert a future revenue stream and freeze it within the community before pen touches paper. Goodwill simply serves as the vehicle of choice to shoe horn what is undeniably future income back within a community. The accounting buzz and methodology disputes

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133. *Chandler v. Chandler*, 32 P.3d 140, 149 (Id. 2001) (emphasis added). As contrasted to Frantz and Dagan, Justice Eismann, found that “[a] spouse’s knowledge, background, talents, abilities, reputation, work ethic, and so forth are not community property, *even if they were enhanced during the marriage.*” *Id.* (emphasis added).

134. Frantz and Dagan, *supra* note 23, at 107.

135. *Id.* at 107–08.

136. *Id.* at 107. Frantz and Dagan could not consider Louisiana’s Civil Code article 121, “Claim for contributions to education or training; authority of court,” as an acceptable substitute for half of future income. Since article 121 is basically only a recapture of investment expenses and not a share of future profits, perhaps merger and acquisition specialists ought to double as pre-marital counselors?

amount to creating a means to pull the future into the present. This isn't because there is some objectively "correct" way to value a family business or a professional practice during a divorce. The buzz is being employed because it is the *only way to make the future a part of the past*.

Idaho saw seen this conflict between future earnings and present marital property quite clearly, as noted in *Chandler*.<sup>137</sup> Other common law jurisdictions courts have as well. For example, in *Yoon v. Yoon*, the Indiana Supreme Court explicitly held that "goodwill that is attributable to the business enterprise is divisible property, but to the extent that the goodwill is personal to the professional or business owner, it is a surrogate for the owner's future earning capacity and is not divisible."<sup>138</sup> In contrast, the Frantz and Dagan comment explicitly takes the view that future income is divisible by means of calculating its present value.<sup>139</sup>

Proponents of the "professional" or "personal" goodwill concept are pursuing more than some sort of mere reimbursement. Frantz and Dagan see the ex-spouse's share of post-divorce income as a pure entitlement. They reject any sort of return on an investment contributed towards the education of the professional spouse by the non-professional spouse.<sup>140</sup> They believe that, since

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137. *Chandler*, 32 P.3d 140.

138. *Yoon v. Yoon*, 711 N.E.2d 1265, 1265 (Ill. 1999). *Yoon* expressly rejected a ruling made just eleven years earlier, *Porter v. Porter*. *Porter* held that "a professional practice's goodwill value may be included in the marital estate for purposes of property distribution pursuant to a dissolution decree." *Porter v. Porter*, 526 N.E.2d 219, 225 (Ind. Ct. App. 1988). However, the *Yoon* court stated, "To the extent that Porter suggests that both personal and enterprise goodwill are to be included in the value of a business or professional practice in a dissolution, it is disapproved." *Yoon*, 711 N.E.2d at 1269.

139. In fairness, they do acknowledge the "serious intrusion on exit by placing a heavy and unjustified burden on future decisions concerning one's career," something that creates an obvious tension between the ideal of a "clean break" and future career planning. Frantz & Dagan, *supra* note 23, at 111-12 & nn. 160-61. Frantz and Dagan are also aware that apportioning future income not only interferes with "autonomy" but can create a perverse incentive to not work as hard. *Id.* See also *id.* at 107 n.143 ("Encumbering spouses' future career choices in such a way is inconsistent with a commitment to no-fault divorce.").

140. Early efforts to capture future professional income sought to have the legal or medical license itself declared community property. *Muckleroy v. Muckleroy*, 498 P.2d 1357 (1972), a New Mexico case, was such an attempt. The court ruled a license to practice medicine "cannot be the subject of joint ownership." *Id.* at 1358. Spaht and Hargrave's "What Assets Are Shared?" discussion, closely tracks New Mexico's treatment of this medical license. See Spaht & Hargrave, *supra* note 15, § 2.8. Both acknowledge that a license is a protected property right in one context while neither sees that same license as "property" in a community property context. Even Frantz and Dagan concede that "a spouse cannot sell her professional degree," and go on to cite a case with that holding, *In re Marriage of Graham*.

[a]limony is associated with need . . . [it] unjustifiably diminishes a spouse's entitlement to the other's increased earning capacity . . . [A]ssociating [an alimony] . . . claim to this marital asset with dependency . . . sends the wrong cultural message . . . [since, if] each spouse is entitled to the other's increased earning capacity, he or she should not forfeit these entitlements on remarriage, or because of hard work or simple good fortune.<sup>141</sup>

Naturally, the whole reimbursement issue can only revolve around degrees or licenses acquired after marriage. But what about a doctor, lawyer, or engineer who marries only after graduation? In that event, what is the basis for a claim by the other spouse for increases in earning ability during the marriage?<sup>142</sup>

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Frantz & Dagan, *supra* note 23, at 107 & n.151 (citing *In re Marriage of Graham*, 574 P.2d 75, 77 (Colo. 1978)). Of course, some states, Louisiana among them, have either statutes or case law that explicitly allow the non-professional spouse to recover the educational or training expenses furnished to the other spouse. *See, e.g.*, La. Civ. Code art. 121. However, the comments to Louisiana Civil Code article 121 make absolutely clear that no license or degree is ever community property under any circumstances. Article 121, with its caption, reads:

121. Claim for contributions to education or training; authority of court

In a proceeding for divorce or thereafter, the court may award a party a sum for his financial contributions made during the marriage to education or training of his spouse that increased the spouse's earning power, to the extent that the claimant did not benefit during the marriage from the increased earning power.

The sum awarded may be in addition to a sum for support and to property received in the partition of community property.

Moreover, a license or degree holder reimbursing the community for the expense of getting that license or degree is fairly consistent with the "title-finance" distinction that the French follow. The comments to articles 121 through 124 do not refer to the French "title-finance" doctrine because the two concepts are not quite on point. Interview Saul Litvinoff, Reporter for the Civil Code (Oct. 20, 2003). However, it is arguable that the operational effect of articles 121 through 124 is to codify something similar to that French doctrine in Louisiana law.

141. Frantz & Dagan, *supra* note 23, at 108–09.

142. If a purely economic, but nonetheless polite, term describing behavior such as remaining "entitled" to a portion of an ex-spouse's future income after divorce is needed, "rent seeking" might suffice. Rent seeking "consists of legitimate, non-voting actions that are intended to change laws or administration of laws such that one individual and/or group gains at the same or greater expense to another individual or group." J. Patrick Gunning, *Understanding Democracy, An Introduction to Public Choice* Chap. 16. Another definition is "[t]he expenditure of resources in order to bring about an uncompensated transfer of goods or services from another person or persons to one's self as the result of a 'favorable' decision on some public policy." Leon Felkins, *Rent-Seeking Behavior*, at <http://www.magnolia.net/~leonf/politics/rentseek.html>. Felkins observes:

The term seems to have been coined (or at least popularized in

Third, if “a spouse’s knowledge, background, talents, abilities . . . and so forth” are “separate property,” as previously observed in *Chandler*, there is nothing for a court to divide. If that is so, then the value of any goodwill not attached to a business—be it high, medium, or low; professional or personal—is irrelevant. If that is so, the “difficult to value” limitations of accounting and economics become irrelevant. The impossibility of fulfilling a task becomes irrelevant once the attempt to perform the task is abandoned. Or, as Gertrude Stein (of Oakland, California) once said, “There’s no ‘there’ there.”<sup>143</sup>

No part of this comment quarrels with any battle of expert opinion about the goodwill, going concern aspects, or non-compete features in the sale of a business *per se*. Neither is any difficulty in arriving at the value of a business at issue here. No one goes to a hot dog stand because of the reputation of the cook. General Electric is going to sell light bulbs and jet engines to people watching NBC television shows who have never heard of Jack Welch and could not care less who he is. Whatever brand name loyalty or location premium or any other intangible may attach to some business really is something accountants can dispute in an arm’s length commercial transaction. However, when it comes to determining the present value of the increased skill with a pen, trowel, gavel, carpet iron, or scalpel that Tom, Dick, or Harriet managed to pick up while married, the whiff of an old auction block is in the air.

There is no avoiding the issue: because the common law concept of goodwill neither arose from a rigorous taxonomy nor resides within one, it (a) merges distinct issues, (b) muddles and blurs key differences, and (c) does not consider at least two of the obviously foreseeable configurations in the sale of a business.<sup>144</sup> The care of and feeding of goodwill in property settlements has thus become a hopeless muddle of opposite and illogical results across these United States. For example, a recent casenote from Idaho pondering an inconsistent holding by that state’s Supreme Court suggested that “courts must . . . first decid[e] whether goodwill exists due to marketability or . . . because [of] . . . value to the owner . . . by

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contemporary political economy) by the economist Gordon Tullock. Examples of rent-seeking behavior would include all of the various ways by which individuals or groups lobby government for taxing, spending and regulatory policies that confer financial benefits or other special advantages upon them at the expense of the taxpayers or of consumers or of other groups or individuals with which the beneficiaries may be in economic competition.

*Id.*

143. Everybody’s Autobiography, Chap. 4 (1937).

144. The two foreseeable configurations are “introduction” and “clientele.” For a treatment of both, see *infra* Part II.E.1.

looking to the facts of the particular case. Once these determinations are made, the valuation method applicable to the case becomes evident and less confusion will result."<sup>145</sup>

Adopting a doctrinally sound scheme with more precise and realistic definitions avoids most, if not all, of the confusing and inconsistent outcome that was the central theme of the *Chandler* casenote.<sup>146</sup> As stated previously, the proper place to begin an inquiry into the partitioning of goodwill is whether or not this "goodwill" even constitutes a "thing" within the legitimate scope of a court to divide. Only if the goodwill is community or marital property is there any need to inquire further. Instead, the current common law concept of goodwill in divorce actions has "grewed like Topsy," coming to understand—without conscious plan or design—that two sources create goodwill, "enterprise" and "personal," and that these sources produce two types of goodwill, "commercial" and "professional." This is the dominant understanding of "goodwill" in the common law-based jurisdictions of the United States, essentially all states but Louisiana.

The Frantz and Dagan comment is simply the latest in a series of legal articles furnishing a legal rationale for the effects produced by importing accounting and economics concepts into family law. Again, some legal theory was required to support awarding future income as part of divorce settlement outside of alimony.<sup>147</sup> The plaintiff's bar simply discovered what an alteration of goodwill would do before the academics found that marriage could host an "entitlement" to half of all post-divorce income.<sup>148</sup> Parkman pinpoints a 1956 California case as the initial "deterioration" of goodwill when *Mueller* held that goodwill also existed in the "personal service" of a dental laboratory.<sup>149</sup> By 1974 in California, an

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145. Courtney E. Beebe, *The Object of My Appraisal: Idaho's Approach to Valuing Goodwill as Community Property in Chandler v. Chandler*, 39 Idaho L. Rev. 77, 109 (2002). See also *Chandler v. Chandler*, 32 P.3d 140 (2001).

146. Beebe objected to *Chandler* because it used a different method to calculate goodwill. Prior to *Chandler*, goodwill in Idaho divorces was measured by what an outsider would pay for the family business. *Chandler* also allowed the goodwill to be valued by its worth to the spouse allocated the business by the court. This latter approach was the one used by Louisiana in *Ellington*.

147. Miod challenges the propriety of such "double dipping," saying, "[c]harging one party in a marital dissolution with the community property goodwill and using the same earnings to compute spousal support is counting the same income twice." Donald John Miod, *The Double Dip in Valuing Goodwill in Divorce* 10, available at <http://www.expertlaw.com/library/attyarticles/Assets/double-dip.html>.

148. See Frantz & Dagan, *supra* note 23, at 108–09 n.139 (strongly advocating the "entitlement" point of view).

149. Parkman, *A Systematic Analysis*, *supra* note 23, at 3 (citing *Mueller v.*

expert witness could be "asked to determine the fair market value of goodwill of a medical practitioner, not of his business."<sup>150</sup> *Foster* regarded "the personality of the parties engaged in the business" as a factor in that property settlement.<sup>151</sup> However, despite the broadening scope of goodwill, many states do not apply the newer definitions in family law cases. As will be shown in Part III.B., there is considerable disagreement over what is "marital property" (in states whose laws flow from the common law tradition) as well as what falls into a community regime (in community property states).

By contrast, as will be next demonstrated in Part II.E., the civilian tradition of clientele encompasses everything that the common law usually considers as either "enterprise" or "commercial" goodwill as well as additional features that the common law does not consider. Moreover, the civil law treats both "personal" and "professional" goodwill in a radically different way.

#### *E. Clientele in the Civilian Tradition as Seen in Contemporary French Doctrine*

The emphasis is "contemporary." The comprehensive reform of June 13, 1965 understandably had a wide ranging effect on family law in France, provoking much debate among scholars.<sup>152</sup> The discussion of clientele and its effects in Parts II.D.1. and II.D.2. is based upon three sources reflecting this spirited debate: (a) present French law, which is still the June 13, 1965 package of *Code Civil* articles; (b) the majority position among today's French legal scholars ("juriscounsels" or "jurisconsults" in civilian terms) interpreting the 1965 laws; and (c) Professor Trahan's unpublished survey of the pertinent community property law as it developed in France from the mid-19th century to today. Many of the policy arguments typified in the Frantz and Dagan comment arose within France around the time of *Smith v. Everett*, more than a full century ago, although French scholars sympathetic to the Frantz and Dagan view did not begin

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Mueller, 301 P.2d 90 (1956)).

150. *Id.* (citing *Foster v. Foster*, 42 Cal. App. 3d 577 (1974)).

151. *Id.* (citing *Foster*, 42 Cal. App. 3d at 583).

152. Due to time, language, and budget constraints, this part of the comment does not attempt to cover the development of French law and doctrine concerning clientele in anything like the depth devoted to the parallel development of goodwill in England and the United States. All of the doctrinal sources in Part II.E. were translated from original French works by Professor J.R. Trahan of the LSU Paul M. Hebert Law Center. Additionally, Professor Trahan's unpublished brief survey of French family law over the last 150 years was instrumental in composing this "mini-introduction" to clientele [hereinafter Trahan Survey].



"tout[ing] . . . in earnest [that] . . . approach" until more recent times.<sup>153</sup>

*1. Scope and Meaning of the Civilian Term "Clientele"*

The present day understanding of the civilian term "clientele" flows primarily from two articles in the French Civil Code, their *Code Civil*. The first is article 1404, which reads, in pertinent part,

[The following things] constitute separate things by nature, even when they have been acquired during the marriage, . . . the clothing . . . personal . . . to one spouse, personal injury awards, . . . and, more generally, all goods that have a personal character and all the rights exclusively attached to the person.<sup>154</sup>

The second major article is 1469, which reads, in pertinent part:

Compensation is, in general, equal to the lesser of the two sums than represent the expenditure made [on the one hand] and the subsisting profit [on the other hand]. [Nevertheless, the compensation] cannot be less than the subsisting profit when the value [of community property] that has been borrowed served to acquire, conserve, or ameliorate a good that, at the time of the liquidation of the community, still remains in the patrimony of the borrower [spouse].<sup>155</sup>

The majority of contemporary French scholars writing of clientele as affected by articles 1404 and 1469 recognize it to have two subtypes: "professional" and "commercial." Both are "transmitted in the same way . . . the successor is made to pay for the transferor's presentation of him to the clientele and for the transferor's engagement not to compete with him."<sup>156</sup> In actual daily operation, the "non-compete" aspect of selling a business or profession is not as cut-and-dried as this Marty and Raynaud text suggests. While this "presentation," also known as an "introduction," is a necessary element of all such sales, non-competition does not automatically follow by operation of law. Another pair of doctrinal authors, Aubry and Rau, observe that a common rationale explains why neither "professional" nor "commercial" clientele can be community property. They maintain "present[ing] a successor to the clientele,

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153. Parkman, *A Systematic Analysis*, *supra* note 23.

154. C. civ. art. 1404 (J.R. Trahan trans.).

155. *Id.* art. 1469.

156. Gabriel Marty & Pierre Raynaud, *Droit Civil: Les Regimes Matrimoniaux* No. 181, at 150-51 (2d ed. 1986) (J.R. Trahan trans.).

while engaging [to leave] the profession, constitutes a prerogative that's too personal to be able to fall into the community. . . . One should also regard as personal the right of a business representative or an insurance agent to present his successor."<sup>157</sup> As it happens, in the vast majority of such sales, a non-competition agreement is part of the sale. However, it is neither legally required nor assumed by law in France.<sup>158</sup> It is, however, the common practice.

The French see this "right of introduction" as the key element in the purchase of any business.<sup>159</sup> The seller (vendor) introduces the buyer (vendee) to his former customers, recommends the new owner to them, and—frequently—explicitly pledges not to compete with the new owner. A French buyer isn't paying for the right to get old business repeated. The French vendee is paying for a handoff, for the passing of a baton. The doctrinal problem for civil law with this "right of introduction" did not lie in "May the seller charge the buyer for an introduction?" All the juriscounsels agreed that an introduction to a business was as marketable a thing as was the business itself. No, the problem was more "Must the vendor share the civil fruits (here, money) of the introduction thus sold with his spouse?"<sup>160</sup> The fairness of designating all the money received from a "passed baton" as solely the separate property of the professional (or the commercial) spouse has troubled commentators (although a minority) in France for a century. They argued that strictly personal things must be extra-patrimonial; things without pecuniary value. If money changes hands for this right of introduction, then surely at least some portion of that money must necessarily be patrimonial—how could money be otherwise?—and thus at least some of that money must necessarily fall into the community. The search for a theoretical foundation to justify placing a share of these professional and commercial introductions into the community eventually settled upon a late eighteenth century formulation, the *titre-finance* pair.<sup>161</sup>

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157. 8 Charles Aubry & Charles Rau, *Cours de Droit Civil Francais* No. 166, at 296–98 (Paul Esmein & André Ponsard rev., 7th ed. 1973) (J.R. Trahan trans.). Again, despite the apparently clear text of Aubry and Rau, a non-competition agreement is not automatic under French law.

158. Trahan Survey, *supra* note 152, at 3. Nonetheless, both civilian tradition in general and Louisiana in particular provide that "custom" is a source of law. *See, e.g.*, La. Civ. Code art. 1. "Custom results from practice repeated for a long time and generally accepted as having acquired the force of law." *Id.* art. 3. However, custom "may not abrogate legislation." *Id.* *See also id.* cmt. d ("In all codified systems, legislation is the superior source of law."). Thus, at some point, custom can reach a "tipping point" and become law.

159. Trahan Survey, *supra* note 152, at 2, 3.

160. *Id.*

161. *Id.*

French law originally developed *titre* (title) and *finance* (finance) to deal with a special form of property with an income stream, the "ministerial office." (At the time, some government positions could literally be bought.) If a couple divorced, how should the office be treated? What if the wife had put up most of the purchase price, yet, of course in 1782, the commission was only in the husband's name? The French resolved these questions by holding that the profits of an office, the "finance," were community assets, while the holding of the office and the duties of it, the "title," were strictly personal to the officer holder.<sup>162</sup> Moreover, the non-officer spouse was compensated by the office-retaining spouse for any separate property contributed in purchasing the office. (Adoption of the *Code Napoleon* in 1808 codified these doctrines.)

In modern times, Malaurie and Aynés observe that a type of *titre-finance* distinction has been extended to such diverse civil clienteles as medicine, law, architecture, and insurance. They also note that either of two foundations in doctrinal works would suffice for excluding a professional's personal attributes from the community: the "all-of-a-personal-nature-is-a-separate-thing" school of thought as well as the classic "*titre-finance*" distinction.<sup>163</sup> They go on to cite a *Cour de cassation*<sup>164</sup> decision upholding the "mixed" character of a clientele. In essence, while the proceeds of the sale of a practice fell into the community, the "confidence and free choice of the sick . . . remains attached to his person [the surgeon] and is, therefore, untransferrable."<sup>165</sup>

More than just "doctrine," meaning the writings of (frequently self-described) "eggheads" in the civilian tradition, supports both the "community-separate" and the "finance-title" distinctions. Article 1404 of the French *Code Civil* excludes from the community "all property which has personal character" as well as "all rights exclusively attached to the person."<sup>166</sup> Gérard Cornu writes that the "incorporeal goods" category ("intangibles" at common law) "includes within it ministerial offices and 'clienteles' of liberal professions . . . [because] . . . these incorporeal properties present an accentuated personal character."<sup>167</sup>

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162. Philippe Malaurie & Laurent Aynés, *Cours de Droit Civil: Les Régimes Matrimoniaux* Nos. 365–366, at 167–70 (1988) (J.R. Trahan trans.).

163. *Id.* at 169.

164. The *cour de cassation*, "court of breaking judgments," is the highest French court for some matters, including family law.

165. Malaurie & Aynés, *supra* note 162, No. 366 n.122.

166. Trahan Survey, *supra* note 152.

167. Gérard Cornu, *Droit Civil: Les Régimes Matrimoniaux*, 346–47 (5th ed. 1989).

Some French courts, even prior to the reform of July 13, 1965, had held that the monetary value of the "right of introduction" being sold was a community asset.<sup>168</sup> This is not remarkable, in that all proceeds from the sale of a community business fall into the community. The obvious problem in a divorce, of course, is that the partitioning of a community from a dissolving marriage is not a "willing buyer, willing seller" sale.

## *2. Effects of Clientele on Marriage Dissolution in Civil Law Jurisdictions*

While community property in France consists of the same "goods proceeding from the personal industry of the spouses" as in Louisiana, and such things as "acquets," the acquisitions, fall into a French community just as into a Louisiana one, no French community ever contains any of the personal qualities that produced or earned those goods.<sup>169</sup> This result flows from Articles 1401 and 1404 of the French Civil Code; "rights exclusively attached to the person" are always separate things.<sup>170</sup>

The French concept of clientele produces several effects when a community business is partitioned. First, the French do not confuse the goods obtained by personal industry with the personal industry itself. The goods themselves are community property; they must be divided. If they cannot be divided, they are allocated, with the other spouse receiving a compensating offset. However, the personal attributes producing those goods are never within the community. Second, the French do not mix accounting or tax principles into their matrimonial regimes. Such concepts as "going concern" are not a part of "clientele."

A sound doctrinal foundation makes sorting out the problems of life easier. It is one thing for the spouse retaining a family business to indemnify the other spouse through the community for expenses the two of them incurred when purchasing a clientele or an office during their marriage. It is quite another thing to regard the

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168. *Id.*

169. Louisiana establishes a "legal regime of community of acquets and gains" which "applies to spouses domiciled in this state." La. Civ. Code art. 2334. Louisiana's community property article, in pertinent part, reads:

The community property comprises: property acquired during the existence of the legal regime through the effort, skill, or industry of either spouse; property acquired with community things or with community and separate things, unless classified as separate property under Article 2341; . . . [and] natural and civil fruits of community property . . . .

*Id.* art. 2338.

170. C. civ. arts. 1401, 1404 (Fr.) (J.R. Trahan trans. 1997).

knowledge, skill, or reputation of one person as somehow requiring a reimbursement to the other party for continuing to possess that knowledge, skill, or reputation. Regarding things as "property" when they are not needlessly generates disputes over what "my fair share" should be. The French avoid all of the controversy attached to personal qualities in the United States by not allowing anyone's personal qualities to ever become a "thing to be shared" within the legal arena. Gertrude Stein's "no 'there' there" applies once again.<sup>171</sup> Unfortunately, not all legal systems enjoy the benefits of a sound doctrinal foundation. Part III, Analysis, next examines some of the adverse effects that flow from the doctrinal weaknesses that are the root of the partition problems involving goodwill in modern divorce litigation.

### III. ANALYSIS: TREATMENT OF GOODWILL IN DIVORCE ACTIONS WITHIN BOTH TRADITIONS

Practical considerations (budget, time) and a manageable scope must constrain every disciplined, focused research effort. Since this comment seeks to be useful for practitioners, judges, and scholars in both common law states and in Louisiana, coverage of multiple jurisdiction types is appropriate. In fact, a hyper-technical purist with deep pockets and no calendar could maintain that there actually are at least five possible baseline configurations to evaluate, not two. Rather than only "common law" and "civil law," the purist's five possibilities could be: (1) civil law (for example, France); (2) the original common law (for example, 1890 New York); (3) common law, but with martial property (for example, 1990 New York); (4) common law, but with community property (for example, California); and (5) a mixed common-civil jurisdiction (for example, Louisiana). However, examination of all these possibilities is beyond the scope of this comment.

Instead, this comment endeavors to strike a fair balance between ignoring important distinctions while still capturing for analysis a reasonable portion of the full legal spectrum concerning goodwill. Hence the comment only considers contemporary civil law (here, represented by the legal scholarship of modern France) and common law principles (here, represented by a range of American cases). The Analysis Section, Part III, reaches three of the purist's five possibilities directly and one by proxy. Directly covered are "purist (3) common law, martial property," "purist (4) common law, community property," and "purist (5), mixed common-civil jurisdiction." The proxy is "purist (1), civil law."

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171. See *supra* note 114.

*A. Clientele and Goodwill: Congruent, Analogues, or Quite Dissimilar?*

Clientele can be an analogue of goodwill in at least two ways. Both attach to a business. Both intend to achieve the same goal—repeat business from customers of the old owner—but by a slightly different route. Where a common law business purchaser is paying for the hope that the old customers will remain, a civil law business vendee has bought an introduction to the old customers. The civil vendee automatically obtains that right of introduction without any express demand for it. By contrast, the common law buyer only acquires the goodwill of the firm by expressly including it in the contract. A common law buyer may or may not receive a non-competition agreement. While a civil vendee does not automatically obtain that right, the prevailing usage includes it. Clientele can also attach to a professional practice, although the modern French apply “profession” to many occupations not generally recognized as “professional” in common law states, such as to insurance agencies. To a civilian, the sale of a profession is simply the sale of a business. The “goodwill-clientele” differences are fairly narrow for business or commercial goodwill.

Where the two concepts, clientele and goodwill, do diverge radically is over personal goodwill. The civil law simply has nothing like the “personal” goodwill causing the pronounced split in case law in the United States. Anything strictly personal to one spouse will always be separate property in a civil jurisdiction. It will never be subject to partition as community property. An *Ellington*-type result is not possible in a civil law jurisdiction. By contrast, depending upon state law, a thing as personal as a particular set of names in the memory of one spouse may or may not be a compensable item of community property. Thus, the short answer to the question of Part III.A., “Congruent, Analogues, or Quite Dissimilar?,” is “Always ‘analogue’ for commercial and business, always ‘quite dissimilar’ for personal, and ‘it depends on your domicile’ for professional.”

*B. Common Law-Based Jurisdictions*

*1. Common Law Without Community Property*

Spaht and Hargrave's treatise offers a keen insight into why martial property states have so much more difficulty with the treatment of separate property and “exotic assets” than do community property states. A true community property state must consider three distinct operations: (a) management of the community during the

marriage; (b) transmission of the community upon death of a spouse; and (c) partition of the community assets if the spouses divorce. By contrast, the martial, or equitable, property states only deal with divorces. As a result, community property states more easily "find that exotic assets are marital property" and so can "apply equitable notions."<sup>172</sup>

*a. Mississippi, Represented by Singley v. Singley*

The Mississippi Supreme Court case, *Singley v. Singley*, did not arise from a closely held family business as did *Ellington*, but was a dispute about valuation of a dental practice, not an ordinary commercial enterprise.<sup>173</sup> However, there are several things about *Singley* that merit close attention. First, the Mississippi Supreme Court treated this professional dental practice as though it was a business. Second, it was a case of first impression for them (*res nova*, a "new thing," to a civilian). Third, as the Court surveyed, extensively, the case law from many jurisdictions across the country before ruling, the Justices were well aware of all the arguments and their implications before handing down their ruling.<sup>174</sup>

Mississippi's decision in *Singley* began simply enough, holding that "goodwill should not be used in determining the fair market value of a business, subject to equitable division in divorce cases."<sup>175</sup> However, the key point of a case sometimes lurks in a seemingly minor footnote and that is true here.<sup>176</sup> Footnote 2 of *Singley* contains this gem: "We note that the *Yoon* court distinguished between 'business enterprise goodwill' and 'personal goodwill.' However, the [*Singley*] parties did not mention such terms, much less distinguish them in the record of this proceeding, thus this issue is not before the Court."<sup>177</sup>

The *Yoon* case cited by the Mississippi Supreme Court was a doctor's divorce action in Indiana.<sup>178</sup> The *Singley* court described *Yoon* as "stating that Indiana law adheres to the rule that goodwill based on the personal attributes of the individual is not properly part of the marital estate."<sup>179</sup> *Yoon* was remanded because the lower court

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172. Spaht & Hargrave, *supra* note 15, § 2.4.

173. 846 So. 2d 1004 (Miss. 2002).

174. *Id.*

175. *Id.* at 1010.

176. The most famous such footnote of all must be Justice Harlan F. Stone's note 4 from *United States v. Carolene Products Co.*, 304 U.S. 144, 152 n.4, 58 S. Ct. 778, 784 n.4 (1938).

177. *Singley*, 846 So. 2d at 1010 (emphasis added).

178. *Yoon v. Yoon*, 711 N.E.2d 1265, 1269 (Ill. 1999).

179. *Singley*, 846 So. 2d at 1010.

did not break out “personal” goodwill from “commercial” goodwill. The Indiana district court was instructed to make a factual determination of the personal value component within the total goodwill of the medical practice and to then deduct that amount from the marital property.<sup>180</sup>

*Singley*'s footnote 2 is very important for at least three reasons. First, it graphically demonstrates the difficulty common law practitioners have in realizing effects of the excessively broad and poorly defined term “goodwill” as employed in divorce cases. Second, the “two source, two effects” model cited in the 2002 Idaho case note, and echoed in the articles found for this comment, is an accurate depiction of the common law scheme.<sup>181</sup> Finally, the Mississippi Supreme Court did grasp the implications of confusing different types of goodwill. Their understanding of the key point of *Yoon* is a foreshadowing of why they held personal goodwill is not marital property.

Despite recognizing the “nebulous” nature of the term goodwill in marital property divisions, the *Singley* court saw that “[g]oodwill within a business depends on the continued presence of the particular professional individual as a personal asset and any value that may attach to that business as a result of that person's presence.”<sup>182</sup> Again, any panel of judges hearing this case anywhere within a civilian jurisdiction would see these personal qualities as falling outside the community and thus into the separate property of that person.

However, the *Singley* court next took a position quite incompatible with both the civilian tradition's and the common law's understanding of goodwill as attached to a business. Treating the “value that exceeds the value of the physical building housing the business and the fixtures within the business” as a part of business goodwill is unremarkable.<sup>183</sup> Similarly, there is nothing unusual in observing the difficult and “nebulous” nature of personal goodwill. However, the *Singley* opinion resolves this quandary by “recogniz[ing] that *goodwill is simply not property*,” thus it cannot be deemed a divisible marital asset in a divorce action.<sup>184</sup>

As a matter of law, within both traditions, the “not property” statement simply goes too far. No civilian scholar would say in a doctrinal work that “clientele” is *never* property. No common law treatise would say “goodwill” is *never* property. The foundational

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180. *Yoon*, 711 N.E.2d at 1270.

181. Beebe, *supra* note 145.

182. *Singley*, 846 So. 2d at 1011 (emphasis added).

183. *Id.*

184. *Id.* (emphasis added).



common law cases held goodwill to be property.<sup>185</sup> Every French scholar in Part II.D.1. saw "clientele" as marketable. Lindley in his *Partnership* saw "goodwill" as equally marketable. Rather, goodwill can only be property when (a) something is being sold and (b) that "thing" is neither a person nor a part of a person's personality, as was explained in the review of French doctrine. Thus, any court remanding a *Yoon*-type case should have inserted the word "personal" in that text, so that it read "[t]he difficulty is resolved however when we recognize that personal goodwill is simply not property;" thus it cannot be deemed a divisible marital asset in a divorce action.<sup>186</sup>

*b. New York, Represented by Moll v. Moll*

There is nothing especially noteworthy in the New York case of *Moll v. Moll*<sup>187</sup>—*once one accepts the idea that personal qualities are divisible things*. (But then there is nothing especially noteworthy about "taking a negro to Nebraska," once one accepts the idea that there is "no difference between hogs and negroes.") This case can be read two ways. Perhaps it is only a fairly straightforward construction of a statute by a common law trial court faithfully following the binding precedent of the highest court within that jurisdiction.<sup>188</sup> On the other hand, this case could serve as a bone-chilling example of

185. See *Morgan v. Perhamus*, 36 Ohio St. 517, 522 (Ohio 1881) ("the good-will of a trade or business, *when connected to it*, is property" (emphasis added)); see also *Metropolitan Bank v. St. Louis Dispatch Co.*, 149 U.S. 436, 446, 13 S. Ct. 944, 948 (1893) (holding that goodwill ceases when its underlying business ceases).

186. Readers who doubt this construction are welcome to try their hands at this riddle: "What is the difference between a doctor and a radio station?" If cases such as *KFOX* and *Meredith Broadcasting* were decided correctly, what is the rationale for treating the goodwill attached to an M.D. differently from the goodwill attached to a D.J.? See *KFOX, Inc. v. United States*, 510 F.2d 1365 (1975); *Meredith Broad. Co. v. United States*, 405 F.2d 1214 (1971).

187. 722 N.Y.S.2d 732 (N. Y. Sup. Ct. 2001).

188. Full consideration of the "*jurisprudence constante-stare decisis*" distinction between civil law and common law is beyond the scope of this paper. Suffice it to say, here, that a trial court in France is not "bound" by the *Cour de cassation* in the way that every American trial court is bound by a United States Supreme Court opinion. For that matter, a Louisiana trial court is not bound by the Louisiana Supreme Court in the way that a New York trial court (or a trial court in the other forty-nine states) is bound by that state's supreme court. As Professor John A. Lovett of the Loyola Law School has observed, "the Louisiana Supreme Court has recently reminded the bar and other Louisiana courts that *jurisprudence constante* is only 'persuasive authority' and therefore a Louisiana court . . . 'is never bound by the decisions which it formerly rendered' and 'can always change its mind.'" See John A. Lovett, *Another Great Debate?: The Ambiguous Relationship Between the Revised Civil Code and Pre-revision Jurisprudence as Seen Through the Prytanika Park Controversy*, 48 Loy. L. Rev. 615, 701-02 (2002) (citing *Doerr v. Mobil Oil Corp.*, 00-0947 (La. 2000), 774 So. 2d 119, 129) (emphasis added).

what can happen when laws are passed without either a sound doctrinal foundation or an appreciation of the consequences of expansive language.

The defendant husband was a highly successful stockbroker who was facing two adverse events simultaneously; divorce and changing employers. He argued there was no “thing” to be divided since his “book of business” was not “his property or property at all.”<sup>189</sup> Mr. Moll truthfully reported that Morgan Stanley Dean Witter owned the client files, not he, and thus that he could not take the files with him if he left.<sup>190</sup>

Mrs. Moll countered that an account executive “must nurture and develop a relationship of trust and confidence with the client in order to ensure the future business of the client.”<sup>191</sup> She maintained “the probability that clients will follow . . . [him] . . . no matter which firm employs him . . . is the asset or ‘thing of value’ created during the marriage.”<sup>192</sup> She gave the court an affidavit from another financial services company stating the common industry practice was to pay a recruited broker what amounts to a “signing bonus” based upon the broker’s contacts and history.<sup>193</sup>

The judge noted the close similarity between the “professional goodwill” ascribed to the defendant husband and the *Cruttwell* case considered in Part II.A.1., opining that Mrs. Moll’s “description of . . . [Mr. Moll’s] . . . ‘book of business’ compares favorably with the legal definition of goodwill . . . [i]n the old English case of *Cruttwell v. Lye* . . . .”<sup>194</sup>

Considering the problems stemming from the injection of accounting into the conventional common law concept of goodwill discussed in Part II, it is easy to understand why this trial court agreed with Mrs. Moll’s argument “that defendant takes too narrow a view of the interest claimed to be marital property.”<sup>195</sup> The “[d]efendant’s ‘book of business’ is not the customer accounts maintained by the brokerage house. *It is the personal or professional goodwill acquired by defendant which is the ‘thing of value’ plaintiff seeks to have equitably distributed.* This court is thus asked to decide whether the personal or professional goodwill of a stock broker is marital property as contemplated by Domestic Relations Law section 236(B)(1)(c).”<sup>196</sup>

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189. *Moll*, 722 N.Y.S.2d at 733.

190. *Id.*

191. *Id.*

192. *Id.*

193. *Id.*

194. *Id.* at 734.

195. *Id.*

196. *Id.* (emphasis added).

Once the trial judge concluded that there was a "thing" here classifiable as property, and that neither the personal quality nor the intangible nature of that property barred its division, *Moll* became a simple matter of statutory construction. Did the knowledge, skill, and customer names embedded upon the memory pathways within the defendant husband's brain constitute an item of marital property within the reach of New York's Domestic Relations Law? This judge held that they did, interpreting section 236(B)(5)(e) of the Domestic Relations Law to include "an interest in a profession or professional career potential" as "marital property."<sup>197</sup> The trial court then recited no less than twelve New York cases in which things as diverse as having been an opera singer, once holding a seat in Congress, or being certified to administer a public school had all been held to be marital property subject to partition because of "the 'enhanced earning capacity' which the 'thing of value' provided to its holder."<sup>198</sup>

There is no reasonable way to avoid outcomes such as *Moll* after the passage of New York's Domestic Relations Law and their holding of *O'Brien*. Still, one is reminded of a classic Lincoln cabinet meeting story. "If I call a tail a leg, how many legs does a dog have?" "Five," came the chorused reply. "No," said Lincoln, "four. Calling a tail a leg does not make it one."<sup>199</sup>

c. *New Jersey, represented by Seiler v. Seiler*

Just across the Hudson River lies New Jersey. On facts nearly identical to *Moll*, however, a court of appeal upheld a trial court's ruling that the insurance agent husband had no goodwill.<sup>200</sup> Mrs.

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197. *Id.* The original *Moll* text cited here contains an internal citation to the initial Court of Appeals' (New York's "supreme court") landmark 1985 decision in *O'Brien v. O'Brien*, 489 N.E.2d 712 (N.Y. 1985), interpreting this section of New York's Domestic Relations Law. *O'Brien* requires partitioning the personal goodwill of a professional practice. Curiously, Frantz and Dagan believe "[t]he *O'Brien* court actually went too far," citing with approval a comment by Scott and Scott that *O'Brien's* methodology improperly takes into account "professional experience, skill development, and seniority" that will occur in the future and so is not yet attained or created when the marriage ends. See Frantz & Dagan, *supra* note 23, at 107 n.143 (citing Elizabeth S. Scott & Robert E. Scott, *Marriage as a Relational Contract*, 84 Va. L. Rev. 1225, 1322 (1998)).

198. *Moll*, 722 N.Y.S.2d at 736.

199. Innumerable accounts of this story abound. This one comes from Senate testimony (statement of Roger J. Williams) in 1974: "Lincoln had a conundrum which he allegedly used and it was: If you call a tail a leg, how many legs has a dog? Someone would answer five. But Lincoln said, No, calling a tail a leg doesn't make it a leg. Dogs only have four legs." *Food Supplement Legislation: Hearings on S. 2801 and S.3876 before the Subcomm. on Health of the Senate Comm. on Labor and Public Welfare*, 93d Cong. (1974) (statement of Roger J. Williams).

200. *Seiler v. Seiler*, 706 A.2d 249 (N.J. Super. Ct. 1998).

Seiler argued that the goodwill attached to him at his Allstate agency was a marital asset requiring equitable division.<sup>201</sup> The trial court agreed goodwill was present but found that Mr. Seiler was only an Allstate employee and thus any goodwill belonged to Allstate, not him.<sup>202</sup> That a client might follow him to some other insurance company was not dispositive of the issue. Moreover, Mrs. Seiler did not seek to have the insurance agency assigned as a marital asset. The appeal court could find no New Jersey case recognizing any goodwill not associated with some business entity.<sup>203</sup>

Again, *Moll* can be easily explained by New York's quite stringent Domestic Relations act. However, the *Seiler-Moll* case pair presents another riddle opportunity: "How is a brokerage house that owns its files different from an insurance agency that owns its files?" Messrs. Moll and Seiler were both employees of service businesses where being trusted by the customers was essential to success. Both knew many people, both were trusted by many people; neither owned the files nor the databases in their respective workplaces. So, what is the principled basis for placing the memory, trust, knowledge, and contacts of Mr. Moll within the community while excluding the memory, trust, knowledge, and contacts of Mr. Seiler as separate property not subject to division?

*d. Indiana, Represented by Frazier v. Frazier*<sup>204</sup>

The Indiana case of *Frazier v. Frazier* is very similar to the discussion of *Yoon* in *Singley* because this Indiana appeal court, as did the *Yoon* court, remanded the case with instructions to factor out the personal goodwill and deduct it from the marital property.<sup>205</sup> The other noteworthy feature of this case is how well it displays the inherently problematic nature of the business valuation process.

Mr. Frazier appealed, in part, because the trial court did not "distinguish between personal and enterprise goodwill" and "utilized an improper method for calculating future earnings potential."<sup>206</sup> The experts disagreed on the goodwill's source. One believed their furniture store had scant goodwill without the husband, while the other thought most business buyers would be able to run the store themselves.<sup>207</sup> Since the appeal court could not determine from the record if any portion of the "aggregate value" of their business was

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201. *Id.* at 250.

202. *Id.*

203. *Id.* at 252.

204. 737 N.E.2d 1220 (Ind. Ct. App. 2000).

205. *Id.* at 1226.

206. *Id.* at 1224.

207. *Id.* at 1225.

"attributable to the personal goodwill of" the husband, they remanded the case for a determination of the enterprise goodwill with his personal goodwill excluded.<sup>208</sup>

## 2. *Common Law with Community Property*

This category is as split in the treatment of goodwill in property settlements as are common law states without community property. The gap between New York and New Jersey is about as wide as that between California and Texas. The California-Texas split has been so well explored over the last thirty years or so that some articles deal solely with it.<sup>209</sup> In California, commercial and professional goodwill are both community property.<sup>210</sup> In Texas, neither professional nor personal goodwill falls into the community, but commercial goodwill does.<sup>211</sup>

Smith identifies three reasons why professional goodwill has been so contentious and then gives three ways courts have addressed the issue.<sup>212</sup> Her three reasons are the vagueness of the term, its source from a person, and the difficulty of measuring intangibles.<sup>213</sup> As described by Smith, courts deal with the first problem, vagueness, by not recognizing goodwill as community property, the Texas approach in *Nail*.<sup>214</sup> Other courts, as California did in *Golden*, hold goodwill does have a community value despite having "the touch and feel of separate property."<sup>215</sup> The third approach is represented by a case like *Geesbreght* in Texas (although Smith does not cite that case at this point in her article) where goodwill is part of the community and can thus be divided if, and only if, it exists independently of an individual.<sup>216</sup>

Smith's explanation of the discrepancy between California and Texas is largely based on time. Did a court look "backward to when the goodwill was developed or forward to when the goodwill will be realized[?]"<sup>217</sup> The "backward" orientation weighs heavily upon the

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208. *Id.*

209. See, e.g., Catherine T. Smith, *Two Community Property States Differ on its Characterization and Division*, 11 J. Contemp. Legal Issues 246 (1997).

210. See *Golden v. Golden*, 75 Cal. Rptr. 735 (Cal. Ct. App. 1969) (sole medical practitioner); *Todd v. Todd*, 78 Cal. Rptr. 131 (Cal. Ct. App. 1969) (law practice).

211. See *Nail v. Nail*, 486 S.W.2d 761 (Tex. 1972) (personal/professional goodwill arising from a doctor's divorce); *Geesbreght v. Geesbreght*, 570 S.W.2d 427 (Tex. Civ. App. 1978) (commercial goodwill arising in the medical field).

212. Smith, *supra* note 209, at 246-47.

213. *Id.*

214. *Id.* at 247.

215. *Id.*

216. *Id.*

217. *Id.*

"spouses during marriage contribut[ing] to each other's development" such that "the reputation of the individual professional spouse was developed to some extent during the course of the marriage" right along with any other co-owned asset increasing in value during the marriage.<sup>218</sup>

On the other hand, Texas, in Smith's view, instead has something of a "forward" orientation and so is "focused on the future earnings the professional will derive in continuing his or her professional occupation."<sup>219</sup> Of course, if goodwill "is attached to . . . future earning capacity" then it cannot fall into a community today because this future income will arise only after the marriage, and therefore also the community, is no more.<sup>220</sup>

The "today or future?" aspect of goodwill was not the only reason Texas rejected the California view.<sup>221</sup> Smith saw Texas drawing the classic "attached to a business, not to a person" distinction in *Geesbreght*.<sup>222</sup> The view of goodwill in *Geesbreght* is completely consistent with the nineteenth century *Cruttwell* and *Smith* cases in England. Although the facts are radically different, all three cases revolve around a concept of goodwill being bound up in business and not part of someone's personality. In essence, *Geesbreght* involved a corporation, not a person.<sup>223</sup>

In early 1974, Dr. John Geesbreght worked for a company supplying doctors for hospital emergency rooms.<sup>224</sup> He eventually became the half owner of a successor corporation to his original employer. By the time of the divorce in 1977, that company had grown so large (ten full time and between fifty and one hundred part time physicians) and so successful (contracts with eight hospitals) that it was grossing more than \$1,000,000 a year in billings.<sup>225</sup>

The pertinent contested issue before the Court of Civil Appeals of Texas, Second District, Fort Worth in *Geesbreght* was the trial court's failure to include the corporation's goodwill in the property

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218. *Id.* at 247–48.

219. *Id.* at 248.

220. *Id.* Frantz and Dagan agree with Smith on the effects of community termination. See Frantz & Dagan, *supra* note 23. They joined in the criticism of *O'Brien*. See *supra* note 197.

221. Smith, *supra* note 209, at 248. The better view of "time" as an explanation for the treatment of goodwill in court is that "time" is yet another example of an error in legal logic induced by importing accounting and economics terms into law. See *infra* Parts II.C. and II.D.

222. Smith, *supra* note 209, at 248.

223. *Geesbreght v. Geesbreght*, 570 S.W.2d 427, 429–32 (Tex. Civ. App. 1978). The custody dispute over the two children and the jurisdictional questions about the actions in Illinois are outside the scope of this comment.

224. *Id.* at 434.

225. *Id.* at 434–35.

settlement. On remand, the panel held that the company itself enjoyed a certain amount of goodwill value and was "therefore an asset which would have value . . . apart from John's person as a professional practitioner."<sup>226</sup> Thus, "[i]t is clear that in the event John sold his stock to another physician then save perhaps at Harris Hospital there would be an opportunity to retain the contracts of [the company] if the services of its employed physicians in the various emergency rooms continued to be satisfactory."<sup>227</sup> Either Lord Eldon or Sir John Romilly could have rendered the *Geesbreght* opinion. Neither would have experienced any difficulty following its legal reasoning.<sup>228</sup>

While *Geesbreght* has earned, at a minimum, a measure of grudging respect from supporters of the California cases, *Nail* has been fiercely criticized.<sup>229</sup> Mauldin, in a 1981 Tulane Law Review comment, took great exception to *Nail*, primarily because of its focus on the vesting of future income.<sup>230</sup> This 1981 Tulane comment does not contain a single Civil Code article, a single citation to civilian doctrinal work, and confines its historical research to a single quotation, Justice Story's celebrated 1841 treatise on partnership.<sup>231</sup> Even there, this is the full extent of the discussion of that definition: "In the area of professional goodwill, courts have repeatedly relied on the definition by Justice Story."<sup>232</sup> What should have been a glaringly obvious disconnect between "an advantage or benefit . . . acquired by an *establishment*" and the personal characteristics of an *individual human being* somehow escaped the attention of those in the publication review cycle.<sup>233</sup> Moreover, as was demonstrated earlier,

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226. *Id.* at 436.

227. *Id.*

228. *Geesbreght* only cites nine cases, all from other Texas courts, so it followed in *Cruttwell*'s and *Smith*'s footsteps without citing them. Nonetheless, note the unmistakable feel and flavor of *Cruttwell* in the phrases "opportunity to retain the contracts" and "if the services of its employed physicians in the various emergency rooms continued to be satisfactory." *Id.* A chance, the possibility, not a probability or a guarantee, to retain the old customers . . . somewhere Lord Eldon, Sir John, and Baron Lindley are saying "Hear, hear" in unison every time *Geesbreght*'s distinction is seen.

229. See Spaht & Hargrave, *supra* note 15, § 2.8 nn. 27–28 (Supp. 2002) (discussing *Geesbreght*); Mauldin, *supra* note 23, at 319–20 (attacking *Nail* as "not convincing . . . reasoning fails . . . even more mystifying . . . even more questionable in light of subsequent Texas cases . . . basic flaw in all of the court's arguments . . . BOGUS ISSUES . . . The *Nail* court's rationale exemplifies the many smokescreens raised . . .").

230. Mauldin, *supra* note 23, at 319.

231. *Id.* at 314.

232. *Id.*

233. *Id.* (emphasis added). Mauldin's 1981 comment can also serve as yet another example of accounting principles distorting law. All of the legal errors

the Justice Story account of goodwill relied upon by Mauldin is the wrong paragraph.<sup>234</sup> Of course, *Nail* is easily defended simply by citing a single line from it: "[The goodwill] did not possess value or constitute an asset separate and apart from his person, or from his individual ability to practice his profession."<sup>235</sup>

Of course, not everyone agrees that goodwill attached to a person and not to a business falls outside the community. That is the true source of the California-Texas split. The inconsistent case law between the two states is not because of a time orientation shift or of the valuation difficulties. It is fundamentally a values dispute. The key text of *Golden* lays out the weight assigned to the value of spousal support during marriage in California. "Under the principles of community property law, the wife . . . [made a] . . . contribution to any of the husband's earnings and accumulations during marriage" and she is therefore "as much entitled to be recompensed for that contribution as if it were represented by the increased value of stock in a family business."<sup>236</sup>

Lay aside, for the moment, the comparatively small scale, tactical problem of equating a person with a business, as *Golden* does. Focus instead on the "big picture." What is really happening when *Nail* meets *Golden*? The dramatic conflict between two primary values, freedom and contract, first seen by an English Lord in 1810 has simply come 'round once again. Mrs. Golden is Cruttwell and Dr. Nail is Lye.<sup>237</sup>

### *C. Louisiana: A Mixed Common Law-Civil Law Experience through the Ellington Case*<sup>238</sup>

#### *1. Issues Presented*

The essential facts of the case were set out in the opening of the Introduction, Part I. The chief value of *Ellington* was its role as a catalyst in enacting Louisiana Revised Statutes 9:2801.2 in the 2003 Regular Session of the legislature (and, a year later, the revision of

flowing from the use of accounting methods described in Part II.C.2. are present in the Mauldin comment.

234. See *supra* notes 38 & 108. The second Justice Story quote both distinguishes professional goodwill from commercial goodwill and further excludes professional goodwill from the "effects or interests" of a partnership. How then could professional goodwill ever form a part of the "effects or interests" of a corporation?

235. *Nail v. Nail*, 486 S.W.2d 761, 764 (Tex. 1972).

236. *Golden v. Golden*, 75 Cal. Rptr. 735, 738 (Cal. Ct. App. 1969).

237. Professor Harvey was right; "there are no solutions . . . only issues that are fought out again and again." Harvey, *supra* note 36.

238. *Ellington v. Ellington*, 36,943 (La. App. 2d Cir. 2003), 842 So.2d 1160.



9:2801.2 prompted by an earlier draft of this comment). The case itself did not break much new ground. The disputed value and nature of NECC's goodwill, appealed by both parties, is the focus of analysis here.

The larger principle that business goodwill falls into the community had been established twenty years earlier in *Godwin*.<sup>239</sup> The trial court's conclusion that a cotton brokerage house is not a professional practice so as to be separate property was treated as unremarkable by the appeal court.<sup>240</sup> The Louisiana Supreme Court chose not to revisit the issue of why goodwill associated only with a natural person should be subject to a community regime when it declined to hear the case.<sup>241</sup>

## 2. *The Holding of Ellington*

The appeal court affirmed the trial court's blending portions of the methodology and computations of each party's experts to partition this community.<sup>242</sup> The trial judge was well within the legitimate range of his authority, the record amply supported the outcome reached, and there was no abuse of discretion. The closest thing to an oddity in *Ellington* is that Mr. Clark (Mr. Ellington's expert) seems to have been the only person involved in the case who fully appreciated that there might not be a "thing" here to partition.<sup>243</sup>

Standing alone, *Ellington* would scarcely be noticeable. Absent the addition of the new Louisiana Revised Statutes 9:2801.2 text, the length of the string cite in a case such as *Moll* would merely increase from "12" to "13," with "co-owned a family cotton brokerage business" joining the list of occupations ("opera singer," "investment banker") justifying partition of personally-derived goodwill in the property settlement of a divorce.<sup>244</sup>

In *Ellington*, the trial court determined that the value of the corporation varied with which spouse received it, the intangible asset of its customer base is included in the value of the business, but neither spouse had proposed a method properly valuing their business.<sup>245</sup> Thus, the trial court was forced to employ features from each spouse's expert testimony to fashion an equal partition of their

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239. *Id.* at 1170 (citing *Godwin v. Godwin*, 533 So. 2d 1009 (La. App. 1st Cir. 1988)).

240. *Id.*

241. *Ellington v. Ellington*, 2003-1092 (La. 2003), 847 So.2d 1269 (writ denial).

242. *Ellington*, 842 So. 2d at 1170-71. Not assigning all of NECC's goodwill to the spouses might also be an oddity.

243. *Id.* at 1164, n.5. *See also supra* note 24.

244. *Moll v. Moll*, 722 N.Y.S.2d 732, 735 (N. Y. Sup. Ct. 2001).

245. *Ellington*, 842 So. 2d at 1168-69.

community property. This was because neither the general principles in the Civil Code nor the jurisprudence sufficiently addressed the valuation of non-professional businesses.

The goodwill was reasonably weighed in *Ellington*, allowing for the case law at the time and without taking into account any civilian doctrine or the precepts underlying personality in Louisiana's Civil Code. (One has to wonder how the court would have ruled if the French doctrinal materials had been before it.) So, in all fairness, based upon the case law it did have, and upon the way Louisiana Revised Statutes 9:2801 read at the time, a reasonable person can defend the overall outcome of *Ellington*.

Additionally, much of this case—in fact, almost all of its analysis—revolved around the standard, ever-present appeal issues of “adequately supported by the record” and “abuse of discretion.”<sup>246</sup> Appellate methodology and civil procedure are vitally important areas of the law and have their proper place. However, there is nothing remarkable in how the appeal court reviewed the findings and judgment below.

The mathematical details and accounting jargon so painstakingly documented in the record at this point in the *Ellington* opinion have no significance to the thesis of this paper.<sup>247</sup> If and only if personal goodwill is subject to the community does valuation arise as a contested issue for trial. If that point is made, *Ellington* simply becomes a carbon copy of *Moll*. (Or, as some wag once observed, “If you don't know where you are going any road will take you there.”) Once a court accepts the idea that a personal reputation falls into the community, coming to grips with “how to partition someone's reputation” becomes necessary. However, the better course of action is to sort out what is and is not community before attempting a

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246. *Id.* at 1165–66.

247. *Id.* at 1164. To simplify review by those readers who might be inclined to check the math or the methodology, Appendix 1 contains the trial court's undisturbed calculations. However, no part of the thesis of this comment is “the wrong valuation method was used” or “the correct valuation method was improperly applied.” The only way to make *Ellington* a math error is to reduce the goodwill of NECC by Ryan Ellington's thirty-seven percent as estimated by Mr. Clark. *See id.* at 1169. The missing eight percent ( $37\% + 55\% = \text{only } 92\%$ ) must have been attributed to Noble III and Denise, since only fifty-five percent was attributed by Clark to Noble and none at all to Peggy. *Id.* By this logic, and accepting the theory that personal goodwill is divisible, the community only owned fifty-five percent of the goodwill of NECC. The other forty-five percent ( $37\% + 8\%$ ) was owned by their now grown sons and daughter. Of course the problem with this scenario is that the offspring did not own NECC—the parents did. The discrepancy lies in “owning” a portion of the goodwill in a business while not owning any of the underlying business. Severing goodwill from a business is incompatible with both the common law's view of goodwill and the civil law's view of clientele.

partition. For example, "[Ms. Meeks, Peggy Ellington's expert business valuator] specifically admitted that her estimated value would be different if the company was acquired by anyone other than Noble Ellington."<sup>248</sup> If the goodwill of the NECC firm was that personal to him, how is his goodwill in the community? Again, the problem with *Ellington* is not that it followed the *Godwin* precedent which distinguished professions from businesses. The problem lies in treating personal service rendered to buyers differently from personal service rendered to patients or clients.

The Court next took into account the "non-competition" aspect of the other Ellington family members remaining in the cotton brokerage field if all of NECC were transferred to Peggy Ellington alone. Nothing prevented any other Ellington family member from opening another cotton brokerage house and recruiting "all of the [old] customer base . . . developed through the years."<sup>249</sup> Even if she "were [actually] capable of operating the business . . . or even if she could hire an experienced cotton buyer, she would almost certainly have no customers" because none of the customer base was attributable to her.<sup>250</sup>

There are two reasons why this whole block of dicta and reasoning could not arise in, say, France. First, under the civilian doctrine of "clientele," Noble and his sons, Ryan and Noble III, would not only have to introduce the ex-wife Peggy to all their clients, but they would likely also have to leave the cotton brokerage business, at least in that area.<sup>251</sup> Second, the high attributed goodwill percentage, ninety-two percent, would lead a panel of civilian judges hearing the case at trial to see Noble's business acumen as personal, hence separate.

The peculiar nature of the goodwill in this case, so closely associated with Noble Ellington, did give the trial court some pause. "The trial court rejected the valuation method of Noble's expert, Carlton Clark, because it did not include a value for goodwill and instead used the capitalization of earnings method espoused by Peggy's expert, Zoe Meeks, into which an amount for goodwill was factored."<sup>252</sup> In its written reasons for judgment, the trial court saw "Noble Ellington [as] the heart of the business. That is one of the difficulties in attempting to use the ordinary meaning of goodwill in

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248. *Id.* Meeks also "readily admitted that her opinion as to value was based upon present management remaining the same." *Id.*

249. *Id.* at 1168.

250. *Id.*

251. Again, a non-competition agreement in the sale of a business or profession, while the usual practice in France, is not binding as a matter of law. Trahan Survey, *supra* note 152, at 3.

252. *Ellington*, 842 So. 2d at 1169.

a community partition. Perhaps the answer is that NECC has an intangible value which should be recognized but simply does not fit the usual definition of goodwill."<sup>253</sup>

As used in innumerable American divorce cases since California's 1956 *Mueller* case, the "usual definition" of goodwill has surely shifted over time. A key theme of subparts II.C. and II.D. was the ever widening gap, and its effects, between goodwill as first laid down by Lord Eldon and goodwill as it is employed daily in family law in the United States today. Carlton Clark, Noble Ellington's expert, first said that there was no goodwill in NECC but later testified "the goodwill is personal and non-transferable without the efforts of Noble Ellington."<sup>254</sup> (Note how well the "without the efforts of Noble Ellington" language fits the civilian concept of "introduction" described in Part II.E.1.) The trial court was not consistent with classic civilian doctrine when it then found that the "designation" of this value as "goodwill" or "simply [an] 'intangible asset' or some other term should not be important."<sup>255</sup> The hallmark of civilian thinking is the classification of things; the structured way of organizing rights and duties.<sup>256</sup> Instead, the trial court focused on what this unclassified, unnamed thing did "to the value of the business, irrespective of its designation. . . . In this court's opinion, there is something which makes NECC a successful business."<sup>257</sup>

The legal problem is that the valuable "something" in *Ellington* is neither a material object, such as a high traffic corner location on a busy interstate, nor an intangible or incorporeal right, such as a trademark, a patent, or a copyright. The "something" here is the unique and personal combination of skill, knowledge, and effort bound up within a particular individual. Since the trial court recognized the limitations of "goodwill" in its conventional business sense, the judge sought a more concrete item that might capture the "something" of value. The trial court determined the valuable thing "being dealt with is the customer base which the company has built through the years beginning in 1979. There is no magic in the term 'customer base' other than it may be free of the restrictive definitions of goodwill."<sup>258</sup>

It is one thing for a common law court to adapt and develop law from the bench as a rule is needed. That is exactly the approach Lord Eldon had to take in *Cruttwell*. A need arose, he fashioned a rule to fit the situation, other judges found the new rule useful, and it became

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253. *Id.*

254. *Id.*

255. *Id.*

256. Tucker, *supra* note 13.

257. *Ellington*, 842 So. 2d at 1169.

258. *Id.*

the law thereafter.<sup>259</sup> It is quite another thing to abandon an old rule without a substitute. Abandoning the "restrictive definitions of goodwill" without a ready concept or doctrine to take its place is rather like departing from a known location without a destination. Reliance upon "customer base" alone cannot be helpful since "customer book" yielded opposite results between *Moll* in New York and *Seiler* in New Jersey.<sup>260</sup> What the trial court did find helpful was Mr. Clark's use of the term "customer base" after he had "den[ie]d" the existence of goodwill.<sup>261</sup> That prompted the court to "review . . . the Louisiana case law relating to goodwill, particularly . . . [concerning partition of] community businesses."<sup>262</sup> In so doing, the judge drew an "essential" distinction between cases holding that goodwill "could not even be considered because of the nature of the business" and cases where goodwill was present and disputed but "the evidence did not establish a separate value based on goodwill."<sup>263</sup> The judge's survey of the Louisiana case law, which was explicitly affirmed by the appeal court, found that "the only businesses . . . excluded from . . . goodwill . . . [by] . . . the nature of the services provided are medical, legal and engineering practices."<sup>264</sup>

However, the combination of Clark's testimony at the trial and the submitted briefs led the trial court to conclude that "apparently Noble Ellington contends that his cotton buying business should also be excluded from having a goodwill value on the same basis as physicians, attorneys and engineers."<sup>265</sup> Ellington's effort to have his personal goodwill treated as a professional practice prompts two observations. First, the French concept of a "profession," what they call the "liberal professions," is far broader than we use that term. They treat an insurance agency just as a medical practice.<sup>266</sup> That

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259. Edgar Bodenheimer, John B. Oakley, & Jean C. Love, *An Introduction to the Anglo-American Legal System* 13 (2d ed. 1988) ("In such a case [referring to situations with either no, or only ambiguous, authority available] the court must articulate and supply a legal norm or principle which will decide the dispute between the parties. Many of the rules and principles of the Common Law and of Equity originated in this fashion.").

260. See *supra* Part III.B.2. Additionally, in Louisiana, the only sources of law are "legislation and custom." La. Civ. Code art. 1. Cases, jurisprudence to a civilian, are not a source of law (at least not according to the Civil Code).

261. *Ellington*, 842 So.2d at 1169.

262. *Id.* Use of case law as primary authority is strictly a common law principle. Despite the conspicuous omission of "cases" from the "sources of law" in Louisiana Civil Code article 1, Louisiana, being a mixed jurisdiction, employs features from both traditions.

263. *Id.*

264. *Id.*

265. *Id.* at 1169-70.

266. See *supra* Part II.E.1 (discussing the doctrinal works of the three pairs of French authors, Marty and Raynaud, Aubry and Rau, and Malaurie and Aynés).

undercuts *Ellington* because Americans tend to see a sharp distinction between a “business” and a “profession.” The French do not; they treat both alike. If they do not, we should not, given our common civil law heritage and the great extent to which our Civil Code originated from France.<sup>267</sup>

Second, perhaps there actually is a truly principled reason, undetected by this research effort, to treat professional goodwill differently than commercial or business goodwill. Still, if this undiscovered but dispositive factor is anything like the “knowledge, skill, or reputation” of the doer of deeds, then wearing a “blue” versus a “white” collar in the work place cannot explain the distinction. “Class” might explain such a distinction but “logic” or “consistency” cannot. Moreover, the distinction cannot be supported within a civil law environment as shown by the French experience. Those who take the position that some “critical mass” of education or skill (or . . . income?) delineates the tipping point for the asset protection found in “professional” status will quickly find themselves forced into making a pair of “sheep” and “goats” lists of occupations.

The *Godwin* case relied upon by *Ellington* nicely illustrates the operational difficulties of separating sheep from goats.<sup>268</sup> The Godwins’ family business was quite similar to the Ellingtons’ family business. In both businesses the husband did the primary work: carpet, drapery and wallpaper in *Godwin*; cotton brokering in *Ellington*. Both wives supported the businesses by such things as running the office and keeping the books. Neither business had large tangible assets. Both wives claimed each business had several hundred thousand dollars of goodwill value.<sup>269</sup> Both husbands contested the goodwill valuation, asserting neither business had such value. The trial court believed Mr. Ellington was attempting to argue that NECC’s goodwill should be disregarded because he rendered a service in the same way that doctors rendered services, which was the

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267. Whether the origins of the Digest of 1808, and hence the proportionate share of Louisiana’s laws, are due to France or Spain has been the subject of much scholarship. However, the “mainly French” or “mainly Spanish” debate over the origin and quantity of code articles by country has no effect on the issues discussed in this comment. See Rudolfo Batiza, *The Louisiana Civil Code of 1808: Its Actual Sources and Present Relevance*, 46 Tul. L. Rev. 4 (1971); Robert A. Pascal, *Sources of the Digest of 1808: A Reply to Professor Batiza*, 46 Tul. L. Rev. 603 (1972). As both countries are civilian, the consequences for *Ellington* should have been the same, had either a civil code or classic civilian doctrine been consulted in that case.

268. *Godwin v. Godwin*, 533 So.2d 1009 (La. App. 1st Cir. 1988), writ denied, 537 So.2d 1165 (La. 1989).

269. See *Ellington*, 842 So.2d at 1163 (noting the Ellingtons’ division of labor), 1170 (describing the Godwins’ division of labor and describing the similarity of the cases).

husband's unsuccessful argument in *Godwin*.<sup>270</sup> Of course, what both husbands were trying to say was that the empty shell of their respective companies had no value apart from their personal skill and effort.

Nonetheless, *Godwin* distinguished "one man 'professional' corporations" from a "commercial business" such as carpet and wallpaper installations.<sup>271</sup> *Ellington's* comparison of its facts with *Godwin's* facts left no doubt that both husbands were "professionals" in a colloquial sense but neither was in any legally recognized sense a "professional." Thus, neither was entitled to exclude goodwill attached to their persons.<sup>272</sup> Specifically, *Ellington* found that a cotton broker's relationship with his customers was more like a carpet installer's customer relationships than a physician's relationship to patients. Thus, *Godwin* was "a 'professional' carpet installer and wallpaper hanger but his relationship with his customers was clearly different from the relationship of a physician to a patient or an attorney to a client."<sup>273</sup>

Actually, the customer relationship was not "clearly different." In *Godwin*, the carpet customers came to Lyn Joseph Godwin, not to "the business," because they trusted *him* and liked *his* work. True, the client relationship was not one of life or death as in medicine but it is based upon the same element of personal trust nonetheless. The same was true of Moll's brokerage customers. The same was true of Seiler's insurance clients. For that matter, the same was true of on-air radio hosts at KFOX. To say that goodwill is somehow "different" because one lays carpet, another sells cotton, while the third fills cavities is uncomfortably close to class as a justification. Moreover, drawing this distinction is not doctrinally sound. As the French sources demonstrate, the hallmark of a "liberal profession" being transmitted by way of the "introduction" is the element of personal service towards a customer base.<sup>274</sup>

Nevertheless, the *Ellington* court found that "NECC can and does have an intangible asset value and whether that intangible value is termed goodwill, customer base or something else is not important. What is important, and also much more difficult, is using that

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270. See *id.* at 1169 ("apparently Noble Ellington contends . . . [goodwill] . . . should also be excluded"), 1170 ("As in this case, the husband claimed . . ."). The latter construction is more forceful and direct.

271. *Id.* at 1170.

272. *Id.*

273. *Id.*

274. Readers who doubt this interpretation must find an alternate way to explain why an insurance agent and a doctor in France each has a marketable clientele and why each performs an introduction as an obligation of the sale.

intangible value in determining the total value of the business.”<sup>275</sup> The Second Circuit affirmed the trial court in both respects; (1) that NECC had goodwill and (2) that goodwill was “predominantly attributable to NECC’s customer base.”<sup>276</sup> Of course *NECC* did not have a customer base. *Noble Ellington* had a customer base. Of course Noble Ellington was not NECC but he, like Lyn Godwin before him, was treated as though he and the company were interchangeable, indistinguishable substitutes for each other. The often heard colloquialism, “I am the company,” became literally, legally true.

Still, in the last analysis, and again based upon what was within the field of view of the trial and appellate courts, a reasonable decision was reached in *Ellington*. Unfortunately for the soundness and logic of the law, reliance upon the confused and degraded concept of goodwill found in today’s common law yielded a result inconsistent with civilian law principles.

#### *D. The Legislative Response to Ellington*

##### *1. Tracking the Language of Senate Bill 844 through the 2003 Regular Session*

Noble Ellington’s waking hours were not confined to the sale of cotton. He also serves as a Louisiana State Senator. As a result of his divorce experience, he introduced a bill to change how the law treats personal goodwill in property settlements.<sup>277</sup> That bill eventually became law, taking effect on August 15, 2003. The second version of the bill appears to have been narrowly tailored to precisely fit the circumstances of Senator Ellington’s divorce. The third and final versions of the bill were quite general in scope.

The original text of Senate Bill 844 included all types of businesses and professions. It did not attempt to factor out “personal” from “business” goodwill.<sup>278</sup> On the plus side, it called out *Cruttwell’s* “old customers will keep coming back” principle, but not limiting goodwill to only that aspect detracted from the bill. As a result, the original Senate Bill 844 would have intensified the muddled current common law understanding of goodwill by including any factor that increases the value of a business beyond its physical assets.

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275. *Ellington*, 842 So.2d at 1170.

276. *Id.*

277. S.B. 844, 2003 Leg. (La. 2003) (original), available at <http://www.legis.state.la.us>.

278. *Id.*



The second version, the “engrossed” bill, was somewhat of an improvement, in that it started to exclude qualities personal to the owner.<sup>279</sup> However, that protection was promptly lost by an excessive limitation, the eighty-five percent ownership exclusion. A better approach would exclude whatever portion of goodwill the fact finder determined as exclusively due to one of the parties. This version most closely reflects Senator Ellington’s personal circumstances.

The reengrossed version was the second amendment to the bill, being the third version of the text.<sup>280</sup> Had this bill become law, Louisiana would be very close to a *Singley*-type position. This bill is still not quite doctrinally sound because its first two lines allow and define goodwill, while the latter lines exclude it. Since this section of the Revised Statutes only deals with community property issues, the better approach would have been to begin with line fourteen as the first line of the new law but reading instead “The community shall not include the intangible . . . .”

The law as finally passed, the fourth version considered, only applies to commercial businesses, excluding professions. Moreover, the use of the word “solely” has profound implications to retaining business spouses attempting to avoid an *Ellington*-type outcome.<sup>281</sup>

## 2. *What if Louisiana Revised Statutes 9:2801.2 Had Been the Law for the Ellington Trial?*

Goodwill is excluded only when it is *solely* due to a personal quality of the owner—to his “identity, reputation, or qualifications” or to “his relationship with customers of the business.” Moreover, under Louisiana Revised Statutes 9:2801.2 as enacted, Peggy Ellington need not show that she had ever been responsible for *any* of the “goodwill” of the business. In *Ellington*, just the testimony of Noble Ellington’s own expert alone would have been sufficient to destroy the “solely” exclusion. Mr. Clark testified that “55% of the customer base of the company is attributable to Noble Ellington and 37% is attributable to Ryan Ellington.”<sup>282</sup> The “solely” exclusion of Louisiana Revised Statutes 9:2801.2 must disappear on those facts. Of course, again based upon the effect of the word “solely,” the eight percent of goodwill left over for Noble III and Denise Ellington (assuming no goodwill arose from Peggy) also destroys the exclusion.

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279. S.B. 844, 2003 Leg. (La. 2003) (engrossed), available at <http://www.legis.state.la.us>.

280. S.B. 844, 2003 Leg. (La. 2003) (reengrossed), available at <http://www.legis.state.la.us>.

281. 2003 La. Acts No. 837.

282. *Ellington*, 842 So.2d at 1169.

The last possibility is that eight percent of the goodwill was attributable to Peggy.

It does not matter which of these three possible sets of allocations a court adopts as correct. All of them will reproduce the identical outcome of *Ellington*. If anyone has any part of the goodwill, “solely” simply cannot apply. That puts all of the personal goodwill back into the community just as though this law had never been enacted. Thus, any trial on similar facts today (any service business whose customer base identifies with one spouse but not the other) should produce the same outcome as *Ellington* despite this new law. In the Louisiana Senate Bill of 2003, the only way a business owner could exclude his personal goodwill from a community business was to demonstrate that he, and he alone, generated one hundred percent of the goodwill attached to that community business.

*3. Has the New Louisiana Revised Statutes 9:2801.2 Resolved the Goodwill Problem in Louisiana?*

No, it has not. Use of the word “solely” in the statute renders the amendment meaning-less. Of course, what *Senator Noble Ellington* wanted—as did a majority of the legislature and Governor Foster—was to prevent all future *Mister Noble Ellingtons* finding themselves in the position of paying their ex-spouses what amounts to ransom for the privilege of being themselves. What is required, either to preclude another partition outcome as Mr. Ellington experienced or to codify the result of a case such as *Singley* in Louisiana (depending upon how much personal interest one may have in the question) is to amend Louisiana Revised Statutes 9:2801.2. Unless the statute is revised to read something like “That portion of the goodwill solely attributable to one spouse will be excluded from the community,” nothing in the law as passed and signed will prevent another *Ellington*-type partition. If the legislature wishes to preclude *Ellington*-type outcomes, Louisiana Revised Statutes 9:2801.2 must either shed or qualify the word “solely.” Part IV.B. makes a comprehensive set of legislative recommendations to correct the “solely” problem.

#### IV. CONCLUSION AND RECOMMENDATIONS

*A. The Superior Civilian Rationale Underlying “Clientele”*

There is no need to change the terminology about goodwill, nor must the existing commercial case law be overturned. Still, these few “modest proposals” would suffice to eliminate much of the

confusion generated by the use of a single term with so many different meanings.

*1. The "Source-Effect" Concept Should Be Abandoned*

Goodwill should only have legal recognition in two varieties, "commercial" and "personal." A working definition for the two terms would combine the best parts of each pair of terms in the present "source-effect" concept. The following meld of generic terms from the world of business valuation and a 2002 casenote could be a good start.<sup>283</sup>

Commercial goodwill attaches only to a business entity itself and consists of both intangibles (such as the reputation of a commercial business or trade partnership, product names, and trademarks) and tangibles (such as retail store and restaurant locations, lists of customers not bound by a contract, and a skilled labor force). Commercial goodwill is distinct from the personal reputation, qualification, or skills of the owners. This commercial goodwill is an asset with a determinable value because it will transfer to the new owner of the business upon the sale of the business to a willing buyer by a willing seller. Sale of a business is automatically sale of its goodwill by operation of law. Goodwill may have a positive, negative, or neutral value. Goodwill may not be purchased apart from the business. The two are indivisible; purchase of either is purchase of both.

In contrast, personal goodwill originates from the individual owner's or practitioner's reputation, knowledge, contacts, experience, skill, or like personal qualities of an individual. It is always attached to that individual and is never associated with any business entity, partnership, or other artificial person. Since the personal qualities of the individual owner, tradesman, artist, or practitioner (such as a doctor, lawyer, engineer, or accountant who holds any required licenses or permits) are the sole source of personal goodwill, this type of goodwill is not subject to any type of forced distribution, partition, or allocation in any proceeding, domestic or commercial.

Nonetheless, and solely at the option and free choice of the individual owner or practitioner, some aspects of personal goodwill may yet be sold or transferred. For example, a non-competition agreement is actually the sale of personal goodwill. An agreement to perform introductions of the new owner of a business to the existing customers or to endorse the new owner are similarly sales of personal goodwill. Violations of agreements by a seller of personal goodwill shall have the exclusive remedies of damages and injunctions. Affirmative specific

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283. These definitions and their effects are drawn from Beebe, *supra* note 145, and from general civilian traditions about personality and the enforceable scope of strictly personal duties.

performance by a seller shall never be a remedy for breach of a personal goodwill contract.

*2. The Goodwill Concept, as Applied in Law, Should Not Be Merged with Either "Going Concern" or "Non-competition" Agreements*

There is nothing improper, and much commendable, with accounting professionals determining amongst themselves how the commercial goodwill of a business entity will be measured or how often it shall be tested for impairment before it can be listed on a balance sheet. Nothing in this comment suggests or requires amending anything in SFAS 141 or 142, nor intends to suggest that Congress revisit the tax treatment of commercial goodwill. By the same token, however, no one's rights, liberties, or property interests should be shoe-horned into some accounting methodology devised in another discipline for another set of reasons. To the extent that property rights are subject to secular authority, that authority must reside primarily in elected and accountable legislatures, not in the deliberations of private bodies standardizing financial reports. The scope of separate property within a marriage simply cannot be a function of bookkeeping, no matter how useful or necessary accounting methods may be within the field of business. Adoption of the following principles as legal guidelines would clarify how limited the concept of commercial goodwill ought to be in a court of law in any jurisdiction:

Principle 1: Commercial goodwill does not presume that the business being purchased is a "going concern." A business need not be a going concern to have goodwill, nor must its goodwill always be positive. A commercial business may have negative goodwill for any number of reasons: its reputation is poor, its retail locations are undesirable, its plant is obsolete, and so on. Principle 2: Purchase of a business does not automatically create a non-competition agreement. Any agreement not to compete must be express, shall be strictly construed, and shall conform to the statutes of that jurisdiction.

*B. Louisiana Revised Statutes 9:2801.2 Should Be Amended to Delete or Qualify the Word "Solely"<sup>284</sup>*

The scope of the initial version of Senate Bill 844 was quite broad. Goodwill applied to "any community owned corporate, commercial or

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284. The 2004 Regular Session of the Louisiana Legislature amended R.S. 9:2801.2 as suggested by this comment, choosing to employ the civilian language rather than the alternate common law version. See 2004 La. Acts No. 177.

professional business” and all three were to be treated alike.<sup>285</sup> Consistent treatment of goodwill, regardless of business form, is in keeping with the civil law’s best and deepest traditions of personality, separate property, and all types of community regimes. There is no principled reason for excluding personal goodwill in professional practices (*Depner, McCarron*) while including it commercial businesses (*Godwin, Ellington*).<sup>286</sup> Happily, building coalitions in the legislature for any particular piece of legislation is outside the scope of this comment. Nonetheless, should the legislature concur that its recent goodwill amendment needs amending, this comment offers a few suggested revisions to Louisiana Revised Statutes 9:2801.2.

One proposed amendment to Louisiana Revised Statutes 9:2801.2 could read:

In a proceeding to partition the community, the court may include, in the valuation of any community—owned corporate, commercial, or professional business, the goodwill of the business. However, that portion of the goodwill attributable to the identity, reputation, or qualifications of the owner or from his relationship with customers of the business shall not be included in the valuation of any type of business.<sup>287</sup>

This text presumes that the business will be awarded to one spouse before the valuation is made. If the valuation is to be made before allocating the business to one or the other spouse, then “owner” should be replaced with “a spouse.”<sup>288</sup>

Another wording could be less specific, replacing the presently enumerated qualities of the spouse receiving the business with more

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285. S.B. 844, 2003 Leg. (La. 2003) (original), available at <http://www.legis.state.la.us>.

286. *Depner v. Depner*, 478 So. 2d 532 (La. App. 1st Cir. 1985); *McCarron v. McCarron*, 501 So. 2d 233 (La. 1987).

287. Those unfamiliar with the Louisiana Civil Code should not focus on the word “his.” See La. Civ. Code art. 3506 (“[T]he terms of law, employed in this Code, . . . shall be understood as follows: 1. The masculine gender comprehends the two sexes, whenever the provision is not one, which is evidently made for one of them only . . .”).

288. There is some dispute as to the significance of the order of the steps in the partition process of Louisiana Revised Statutes 9:2801(A)(4). If the steps are sequential, which comports with the logic of a code, then subsection (a), valuing the assets, must take place before subsections (b), dividing the assets, (c), allocation, or (d), paying of an equalizing sum of money, can occur. While this sequential issue was raised on appeal, the trial court was upheld in its decision to assign NECC first and then value it afterwards. *Ellington v. Ellington*, 36,943 (La. App. 2d Cir. 2003), 842 So.2d 1160, 1170. Because there is some uncertainty on this point, both sequences can be considered, should the legislature choose to amend Louisiana Revised Statutes 9:2801.2.

general language. Articles in the classic codal civilian tradition are usually more general in nature than in the digest format to allow some increased flexibility to judges.<sup>289</sup> Such a text might read:

In a proceeding to partition the community, the court may include, in the valuation of any community owned corporate, commercial, or professional business, the goodwill of the business. However, that portion of the goodwill attributable to any personal quality of the spouse awarded the firm shall not be included in the valuation of a business.

If something like the first wording is adopted, the issue will turn on the expert opinions presented by the contending spouses. Did the wife's personal attributes generate fifteen percent of the goodwill in the company's value? Forty-seven percent? Eighty-five percent? If the second wording is chosen, there will be two points of dispute. The first will likely be a matter of law; what aspects of a person are a "personal quality" and which are not? Once the cadre of judges and doctrinal authors establish what is and is not "personal," the "battle of the experts" will still be joined over how much of the residual goodwill value is "personal" and how much is "commercial."

The choice itself of any remedial approach is something of a value judgment. If the legislature desires to maintain, if not increase, the influence of the civilian tradition in Louisiana, the second wording will be adopted. If not, the first choice will prevail. In any event, if the legislature intends to preclude another *Ellington*-esque partition, Louisiana Revised Statutes 9:2801.2 must either drop the word "solely" or qualify it. If the legislature desires to best honor both the underlying values of the civil law and the autonomy created through

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289. Although it is outside the scope of this comment, the tension between a "code" and a "digest" has been a regular feature of Louisiana's legal history from statehood. There was a Digest of 1808, but a Code of 1825, largely driven by the *Cottin* case of 1817. Vernon V. Palmer, *Death of a Code—the Birth of a Digest*, 63 Tul. L. Rev. 221, 226 (1988). "The present [1988] Revision [of Louisiana's Civil Code] also merits the designation digest because it too is designed to be supplemented by outside sources (codified and jurisprudential), and because the overall ensemble does not have the internal coherence and completeness of a code." *Id.* Moreover, what Professor Palmer forecasts as a crisis "will place in issue the transformed nature of our codification, the judge's increased role as creative rulemaker, the authority of the decided case when it is detached from a legislative base, and the existence of a Louisiana common law that supplements the enacted law." *Id.* There is a good argument waiting to be made that *Ellington's* eschewing the Civil Code and relying only upon cases is both a "detachment from a legislative base" as well as "a Louisiana common law." Future scholars looking for cases to test Professor Palmer's forecast would do well to include *Ellington* in a full test of Palmer's criteria.

centuries of common law development, it will exclude all personal attributes from the community regime.

### *C. A Few Final Reflections*

This comment has been about goodwill in property settlements. However, goodwill disputes do not occur in isolation inside a divorce. Inevitably alimony, spousal support, education credits, child support, visitation, and a host of other issues swirl about in the legal cauldron that is the breakup of a marriage. If one spouse has no other job or career in hand for income after a divorce, the quite understandable temptation is to reach for a larger share of the marital property. Goodwill offers one way to achieve that, particularly when the major source of the value of the family business is a personal characteristic solely attributable to the knowledge, skill, or personal contacts of the other spouse.

In truth, though, the presence or absence of any career potential for the spouse without the contacts or skill is irrelevant. If the business has value largely, if not wholly, derived from a characteristic peculiar to and confined in one spouse, no amount of training or education by the other spouse, or the lack of it, will affect that business value. If customers come to Jane Doe because they like her dress, or her golf course, designs, neither John Doe's having only a second grade education nor his attaining a second Ph.D. will affect the public's desire for Jane's designs. If the value of the "Doe Designs, LLC" is attributable only to her personal characteristics and not to the efforts or knowledge of John, then there is nothing to divide, allocate, or compensate.

Philosophers and marriage counselors can debate—as lawyers and each party's retained business valuers must do today—the intangible contributions of one spouse to the success of the other. Finally persuading your husband, especially after years of effort, to use the word "manure" is a fine thing. However, are such contributions as that refinement something that affects the valuation of a lawyer's practice or a carpet layer's business in any way that a judge can reasonably be expected to determine? Or the value enhancement to some other commercial enterprise? Will any degree of sophistication in an accounting model used to calculate and forecast someone's future earnings ever be able to quantify the proper "compensation" of thirty years of language policing and manure nagging?

Do we really want to (re)define marriage<sup>290</sup> as an institution that confers, *even after its dissolution*, a lifetime “entitlement” to half of another person’s income, regardless of either party’s subsequent circumstances? These are questions beyond the competence of any court to resolve. Requesting what amounts to a flat lien on the future income of your ex-spouse under some variety of an “I contributed at home” rationale comes down to “I want to be treated like a doctor’s wife even after I am no longer a doctor’s wife.”<sup>291</sup>

Ascribing the goodwill attached to a business to a person is the moral equivalent of slavery.<sup>292</sup> Such a practice is acceptable only if we are unwilling to see any difference between “a hog and a negro.” Dividing goodwill based upon a personal characteristic is intellectually the same as seeing no difference between a person and a business. Businesses are things; people are not. Hogs and hard drives are subject to partition; human beings are not.

“Clientele” and “introduction” arise from a superior understanding of the proper scope and meaning of what the common law knows as “goodwill.” Family law must stop its unfortunate reliance upon misapplied accounting concepts and confine the use of goodwill to its original and still legitimate sphere—commercial transactions between willing buyers and willing sellers.

(Mr.) Kelly M. Haggar\*

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290. Concerning the (re)definition of marriage, and the consequences of *Goodridge v. Dep’t of Pub. Health*, 798 N.E.2d 941 (2003), again, this comment is not affected by the “gay marriage” debate. Sex of the other spouse—or, for that matter, the numbers of other spouses—will not affect goodwill. If one person cannot have a property interest in the personality of another person, then it does not matter how many other spouses there can be, nor does it matter how many of them are of which sex. See *supra* note 11.

291. In re Marriage of Ceilley, 662 N.W.2d 374 (2003). See Appendix 2 for the full flavor of *Ceilley*, which nicely bundles many of the issues in this comment within a scant page and a half. A stranger to the institution of marriage would not be able to tell that the relationship described in *Ceilley* and explored by Frantz and Dagan were, in fact, the same legal entity.

292. Frantz and Dagan, *supra* note 23, at 110 n.159, report a case [*Severs v. Severs*, 426 So.2d 992, 994 (Fla. App. 1983)] suggesting that dividing increased earning capacity might be involuntary servitude under the Thirteenth Amendment. This comment argues a moral equivalence to slavery, not a legal one. However, it might nonetheless be possible to develop a legal equivalence to slavery, at least in Louisiana, due to the operational effects of La. Civ. Code art. 2369.3. However, pursuit of that topic is outside the scope of this comment.

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## APPENDIX A

The Second Circuit's Recitation of the *Ellington* Trial Court's Valuation Methodology and Findings for the Noble Ellington Cotton Company, Inc. in *Ellington v. Ellington* 842 So.2d 1160, No. 36,943-CA (La. App.2d 03/18/03), 1164, 1165.

Specifically, the trial court found that:

(a) The standard definitions of "fair market value" in normal accounting practice are not adaptable to the partition of a community—owned business in which one of the parties is allocated the entire business.

(b) The net asset approach used by Carlton Clark is inappropriate in this case.

(c) One of the methods employed by Zoe Meeks—the capitalization of earnings method—is appropriate in this case, but not if based upon a single year's earnings.

(d) NECC has an intangible asset value which supports the use of the capitalization of earnings method.

(e) The determination of "normalized net income" for use in the calculation of the value of the business is appropriate if based upon several years earnings, in this case, 10 years, because the records for that period are available.

(f) Ms. Meeks' calculation of adjustments in arriving at normalized net income is appropriate.

(g) Mr. Clark's calculation of liabilities exceeding tangible assets by \$55,000 is accepted.

In order to use the greatest number of years available to determine normalized earnings, it is necessary to use the 2001 figures from Mr. Clark's report because they are not included in Ms. Meeks' report. Mr. Clark's Adjusted Income Statement Summary shows a loss of \$142,870 for 2001. The court's procedure thereafter (in each case rounding the amount to the nearest \$100) is as follows:

(1) Add the normalized Pre-tax Income (Loss) for each of the years from Ms. Meeks' Income Statement Adjustments. [\$136,700 + \$221,500 + \$220,500 + \$197,000 + \$181,600 + \$217,700 + \$251,900 + -\$347,700 + \$234,200]

(2) Add the adjusted loss figure for 2001 from Mr. Clark's report, as shown above, in order to arrive at a ten year total. [+ - \$142,900]

(3) Add \$18,000 (based upon \$750 per month for the years 2000 and 2001) for expenses paid by NECC but attributable to Ellington-Weaver Cotton Company ("EWCC") as shown on Noble Ellington's amended detailed descriptive list. [+ \$18,000]

(4) Divide the total by 10 to reach the average annual normalized pre-tax income. [ $\$1,188,500$  divided by 10 =  $\$118,850$ ]

(5) Deduct 34% as the estimated provision for income taxes [ $\$118,850 - \$40,500 = \$78,300$ ]

(6) Divide the balance by 22.5% (Ms. Meek's discount rate in calculating today's value of a benefit stream that will be realized over an extended period of time in the future). [ $\$78,300$  divided by 22.5% =  $\$348,000$ ] [FN6]

FN6. The parties have not questioned the 22.5% used by Ms. Meeks.

(7) Deduct the  $\$55,000$  negative net worth calculation by Mr. Clark based on tangible assets. [ $\$348,000 - \$55,000 = \$293,000$ ]

The result is a company value of  $\$293,000$  if the company is allocated to Noble Ellington, and, in that event, the value to Noble Ellington of Peggy Traylor's one-half interest is therefore  $\$146,500$ .

## APPENDIX B

The Court of Appeals of Iowa's Affirmation of the Iowa District Court for Polk County's Findings and Holding in *In re the Marriage of Roger I. Ceilley and Katherine L. Ceilley* 662 N.W.2d 374 (2003)

In fixing the value of the marital estate, the trial court found Roger's share of his medical practice to be worth  $\$303,000$ . Kay challenges this finding because the figure was based only on hard assets, with no allowance for good will. Kay points out that good will can exist in a professional practice for purposes of setting alimony. *In re Marriage of Bethke*, 484 N.W.2d 604, 607 (Iowa Ct. App. 1992); *In re Marriage of Hogeland*, 448 N.W.2d 678, 681 (Iowa Ct. App. 1989). Kay's initial difficulty with this challenge is with the record, which is overwhelming that medical practices in Des Moines are routinely bought and sold with no allowance for good will. Kay confronts this initial difficulty by distinguishing between equity good will, that is good will as we commonly understand it, and personal good will. Citing cases from other jurisdictions, Kay asks us to recognize "equity good will," and distinguish [it] from "personal good will" as a marital asset subject to property division. *Frazier v. Frazier*, 737 N.E.2d 1220, 1225 (Ind. Ct. App. 2000); *Prahinski v. Prahinski*, 321 Md. 227, 582 A.2d 784, 786-87 (Md. 1990); *Hanson v. Hanson*, 738 S.W.2d 429, 434 (Mo. 1987).

But once again Kay is confronted with the record. Roger paid nothing for good will when he acquired an interest in the practice; he is under a contract with his partner associate that specifies good will

should carry no value in the event, for buy-in purposes, of the retirement, debts, or disability of either partner. Both Roger and his partner testified they have an oral agreement that the same provision would apply if either of them leaves the practice for any other reason. Because of Roger's contract with his partner, any "personal good will" that might be assigned to his medical practice is nothing more than a part of his remarkable earning capacity, a matter we have already noted. Although Kay's expert witness assigned an equity good will value to the practice, on our de novo review we agree with the trial court finding that good will has no value as an asset in Roger's medical practice. Because it has no factual basis in the evidence, we need not and do not decide the legal principle the case suggests.

Because it determined Kay had not shown a need for it, the trial court refused Kay's request for permanent alimony. Kay challenges the refusal, contending Roger's enormous earning capacity proves he could readily pay the \$300,000 annually she says would be required to maintain the lifestyle she enjoyed during the last years of the marriage. No doubt Roger has the ability to pay. Kay points out that a \$300,000 award would, after tax consequences are factored, "cost" Roger only \$209,501 which is thirteen percent of his current income.

Alimony is derived from a duty to support. It arises from the ability of one former spouse to pay, and the need of the other to receive. The need exists when necessary to enjoy the standard of living that existed during the marriage. Once that standard is assured, alimony becomes inappropriate.

In former times, alimony served a punitive function, and might have been awarded accordingly without a showing of need. This is no longer true. See Rosemary Shaw Sackett & Cheryl K. Munyon, *Alimony: A Retreat from Traditional Concepts of Spousal Support*, 35 Drake L. Rev. 297, 303-06 (1986).

The record is clear that Kay has no need of alimony. Her average monthly expenditures during the three months prior to trial were less than \$9000. The trial court pointed out that earnings from her half of the marital estate, invested conservatively, would yield several times that—after taxes. When she reaches the age of sixty, the added disposable income from retirement plans will increase dramatically, and will do so again when she reaches sixty-five. The equal division of the vast marital estate, unchallenged on this appeal, was certainly appropriate. It left Kay extremely wealthy. Because nothing more was required to maintain her comfortable lifestyle, alimony was correctly refused.